

***United States Court of Appeals  
for the  
District of Columbia Circuit***



**TRANSCRIPT OF  
RECORD**





BRIEF FOR APPELLANT

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 16,434

125

LEONARD M. ERBCHICK, AND  
LEONARD S. GOODMAN

APPELLANTS

VS.

PUBLIC UTILITIES COMMISSION OF  
THE DISTRICT OF COLUMBIA, AND  
D. C. TRANSIT SYSTEM, INC.

APPELLEES

APPEAL FROM AN ORDER OF THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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United States Court of Appeals

For the District of Columbia Circuit

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## QUESTIONS PRESENTED

1. Did the Commission in its Order and Opinion act arbitrarily, unlawfully, without and contrary to the substantial evidence of record, and without requisite findings, in reaching an end result of a fare well above the national average which burdens transit riders with arbitrary and unreasonable revenue deductions and allows excessive returns on an inflated rate base?

2. Did the Commission depart from requirements of law in proceeding without adequate findings and definite standards, seeking to insulate its order against review by a claim of exercise of "judgment" resting on its own bare conclusion?

The more specific issues in the case, embraced in these broad questions, are reflected in the Statement of Points.

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

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No. 16,454

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Leonard N. Bebchick, and  
Leonard S. Goodman

Appellants

VS.

Public Utilities Commission of  
the District of Columbia, and  
D. C. Transit System, Inc.

Appellees

APPEAL FROM AN ORDER OF THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT OF COLUMBIA



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## SUBJECT INDEX

JURISDICTIONAL STATEMENT . . . . .	1
STATEMENT OF THE CASE . . . . .	2
STATUTES INVOLVED . . . . .	4
STATEMENT OF POINTS . . . . .	4
SUMMARY OF THE ARGUMENT . . . . .	7
ARGUMENT . . . . .	16
I. THE COMMISSION HAS UNREASONABLY AND UNLAWFULLY PERMITTED TRANSIT TO EARN LARGER REVENUES THAN NEEDED TO ATTRACT CAPITAL, RECOUP INVESTMENT, PAY OPER- ATING EXPENSES, AND PROVIDE THE SERVICE, AND HAS THEREFORE BURDENED DISTRICT CONSUMERS WITH UNLAWFULLY HIGH FARES . . . . .	16
II. THE COMMISSION ALLOWED TRANSIT ARBITRARY AND UNREASONABLE OPERATING EXPENSES . . . . .	18
1. <u>The Commission Erred In Its             Allowance of Accruals For Track             Removal And Repaving</u> . . . . .	18
2. <u>The Commission Erred In Allowing             Unlawful Depreciation</u> . . . . .	24
a. <u>Depreciation of Rail Properties</u> . . . . .	24
b. <u>Depreciation of Bus Properties</u> . . . . .	27
III. THE COMMISSION'S ALLOWED EARNINGS OF \$1,143,249 IS UNSUPPORTED BY FINDINGS OR EVIDENCE. FURTHERMORE THE EVIDENCE OF RECORD DOES NOT JUSTIFY A RETURN IN EXCESS OF \$660,000 . . . . .	30
IV. THE COMMISSION ERRED IN FAILING TO ADHERE TO THE RETURN ON RATE BASE AND ATTRACTION OF CAPITAL STANDARDS PRESCRIBED BY STATUTE . . . . .	37



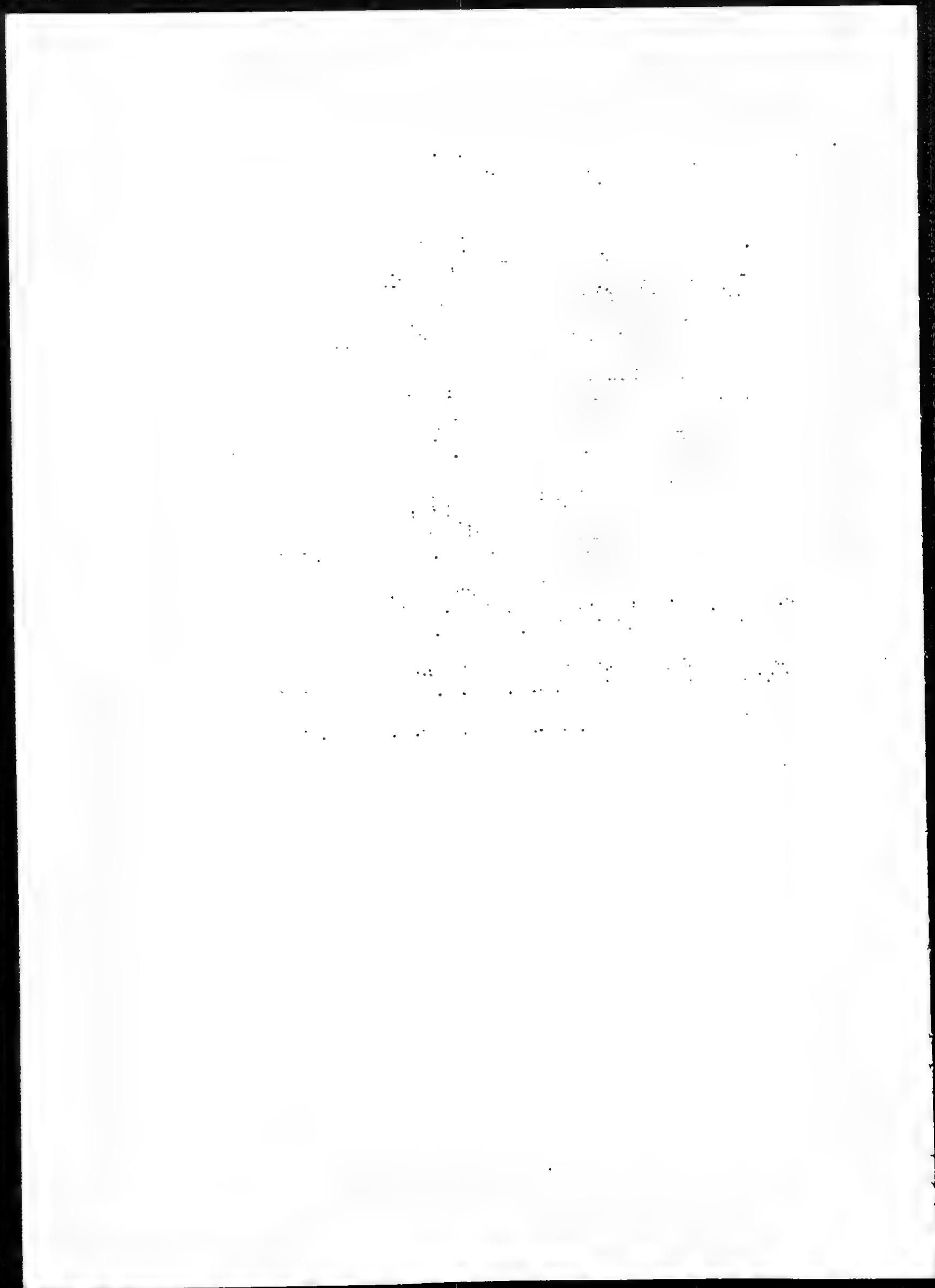
V.	THE RATE BASE MAY NOT EXCEED THE CAPITAL INVESTMENT OF TRANSIT IN ASSETS DEVOTED TO THE PUBLIC SERVICE . . . . .	39
1.	<u>Transit's Return Is Determined By Transit's Investment, Not Another Company's Investment . . . . .</u>	40
2.	<u>Transit's Depreciation Was Ultimately Based On Transit's Purchase Price And It Was Error To Use A Higher Basis For Computing The Permitted Return . . . . .</u>	43
3.	<u>The Commission Erred In Increasing The Rate Base To Take Into Account Any Contingent Liability For Con- version From Streetcar To An All- Bus Operation. The Rate Base Should Have Been Increased For This Item Only As To Amounts Actually Invested By The Company For This Purpose, And Not As To Amounts Obtained From Previous Ratepayers For This Purpose Or For Amounts That May Be Invested At Some Future Date . . . . .</u>	45
a.	<u>Error in increasing the rate base above "purchase price" paid by Transit by averaging with the "original cost" to Capital Transit . . . . .</u>	45
b.	<u>Error in eliminating (through an "amortization" approach) all recognition of the fact that Transit's purchase price was less than original cost to Capital Transit . . . . .</u>	48
c.	<u>Error in referring to track re- moval reserve as a basis for increasing rate base . . . . .</u>	50
d.	<u>Error in using \$10,000,000 "assumed" liability as basis for increasing rate base . . . . .</u>	51





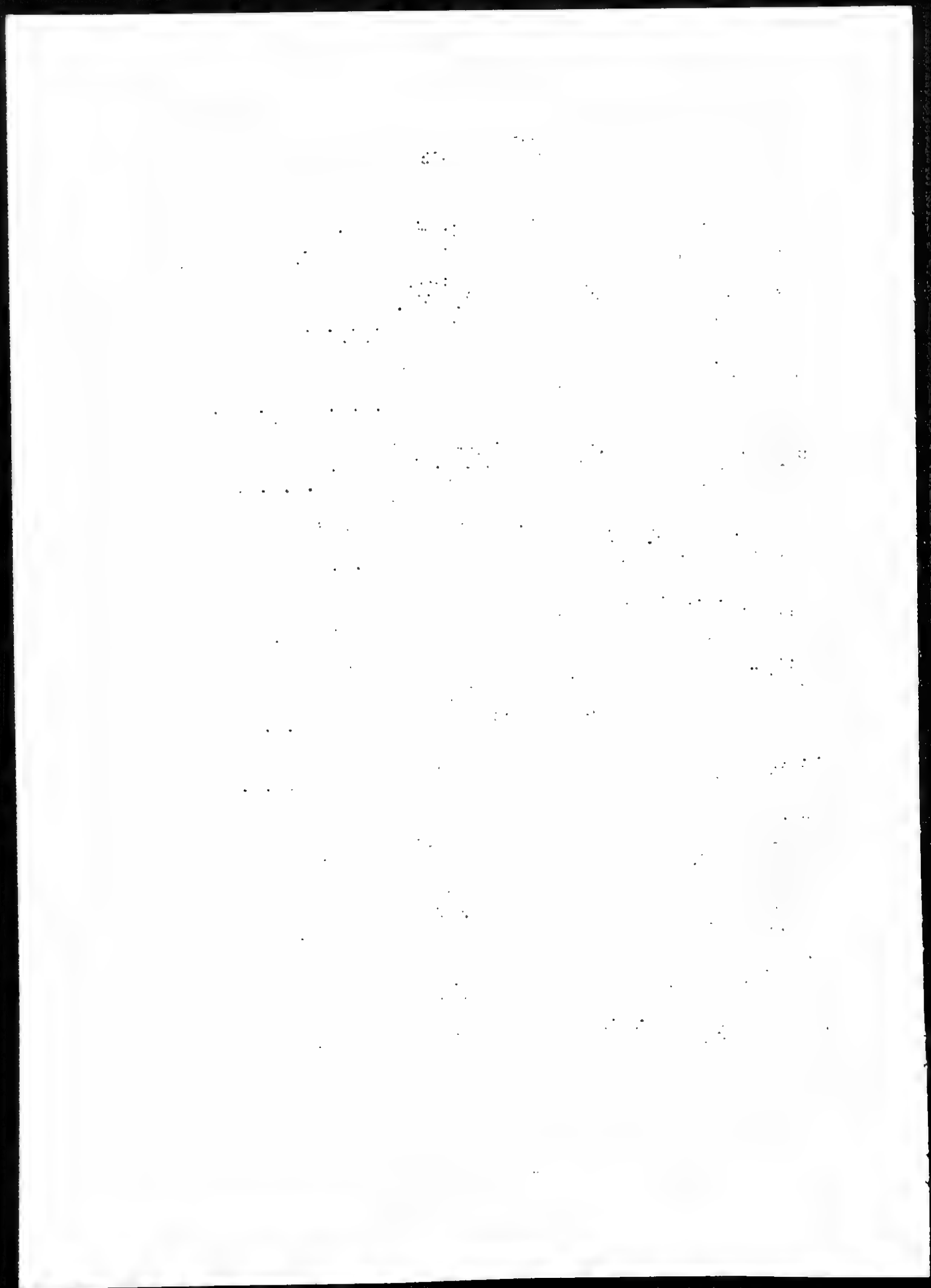


VI.	THE COMMISSION'S VALUATION OF THE RATE BASE AT OVER \$16 MILLIONS IS ARBITRARY, CAPRICIOUS, AND UNREASONABLE . . . . .	52
1.	<u>A Valuation Of The Rate Base At Over \$16 Millions Is Unsupported By, And Is Contrary To, The Sub- stantial Evidence Of Record Which Indicates A Valuation At Around \$12.5 Millions Is Fair And Reasonable.</u> . . .	53
2.	<u>The Commission's Rate Base Of Over \$16 Millions Unlawfully Includes Amounts Which Have Already Been Paid By The Farepayers As Operating Expenses</u> . . . . .	55
3.	<u>The Rate Base Unlawfully Includes Abandoned Properties For Which Transit Has Already Received Full Compensation</u> . . . . .	58
VII.	THE RATE ORDER DERIVES NO SUPPORT FROM THE COMMISSION'S REFERENCE TO A GROSS OPERATING REVENUES METHOD . . . . .	60
VIII.	THE COMMISSION COMMITTED OTHER ERRORS IN THIS PROCEEDING . . . . .	68
	CONCLUSION AND PRAYER . . . . .	70
	APPENDIX A	
	APPENDIX B	

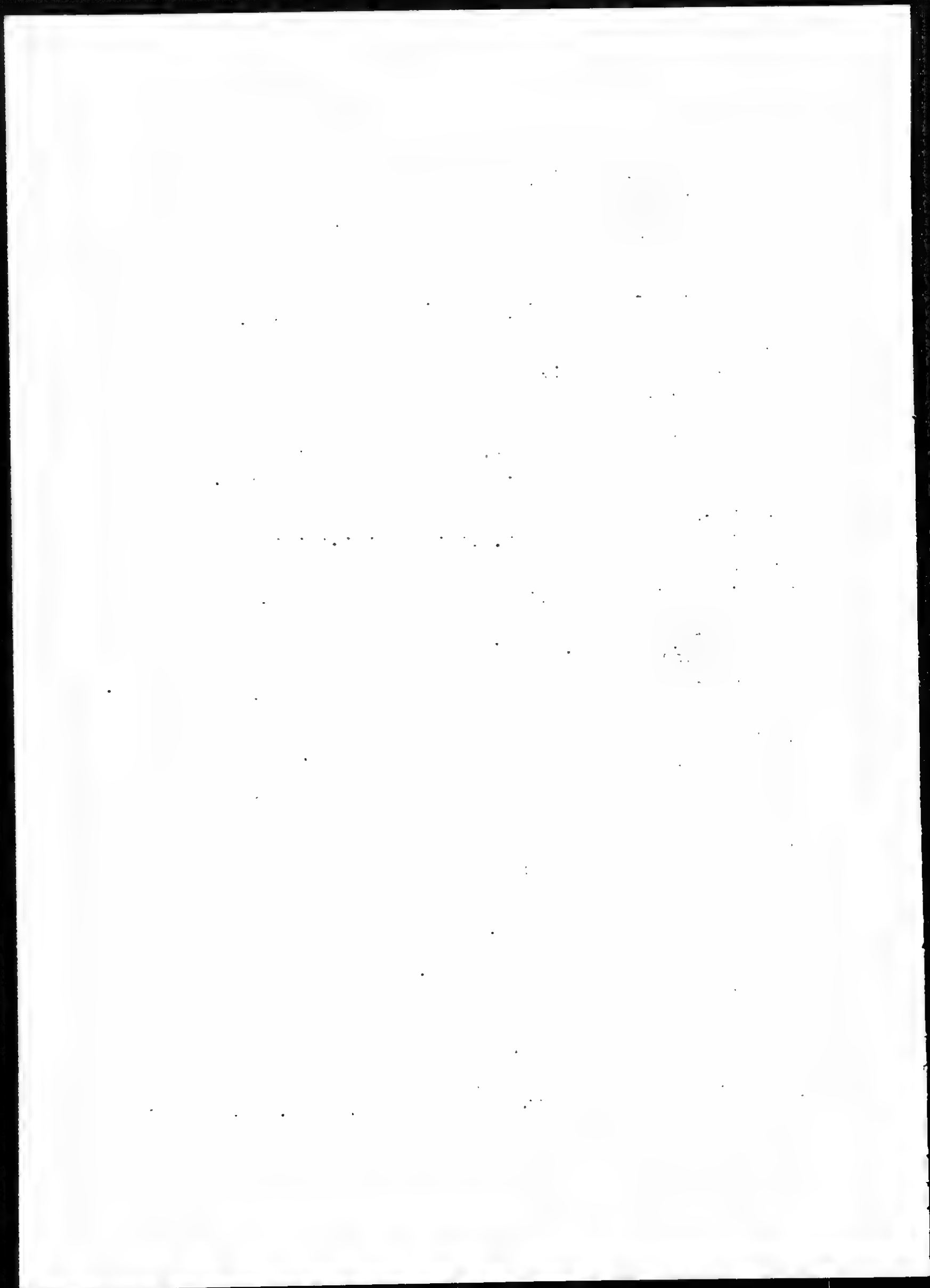


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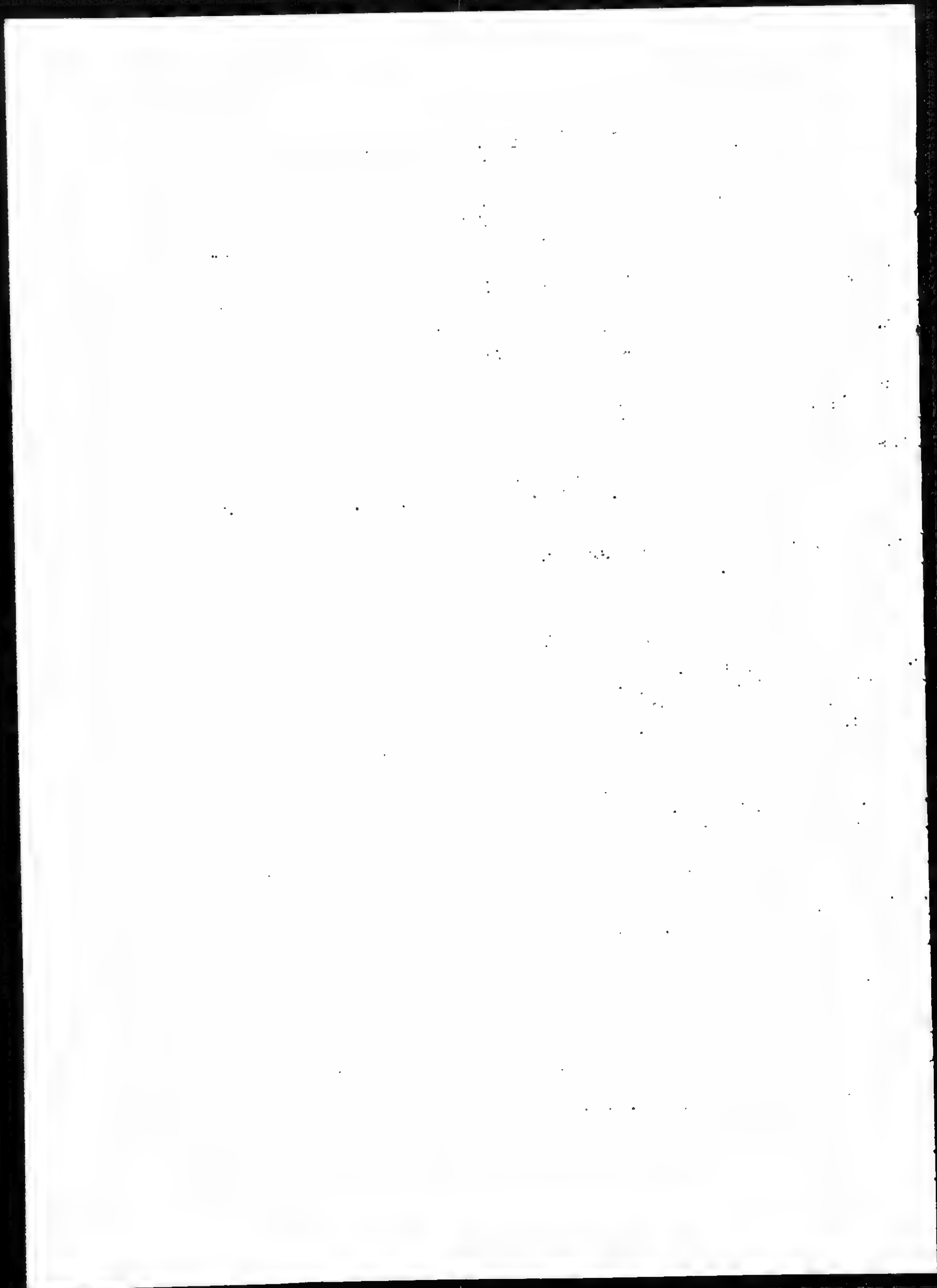


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Section 4 . . . . .	4, 38, 62, 63, Appendix A
Section 7 . . . . .	4, 19, 22, 23, Appendix A
Section 9 . . . . .	4, 63, Appendix A





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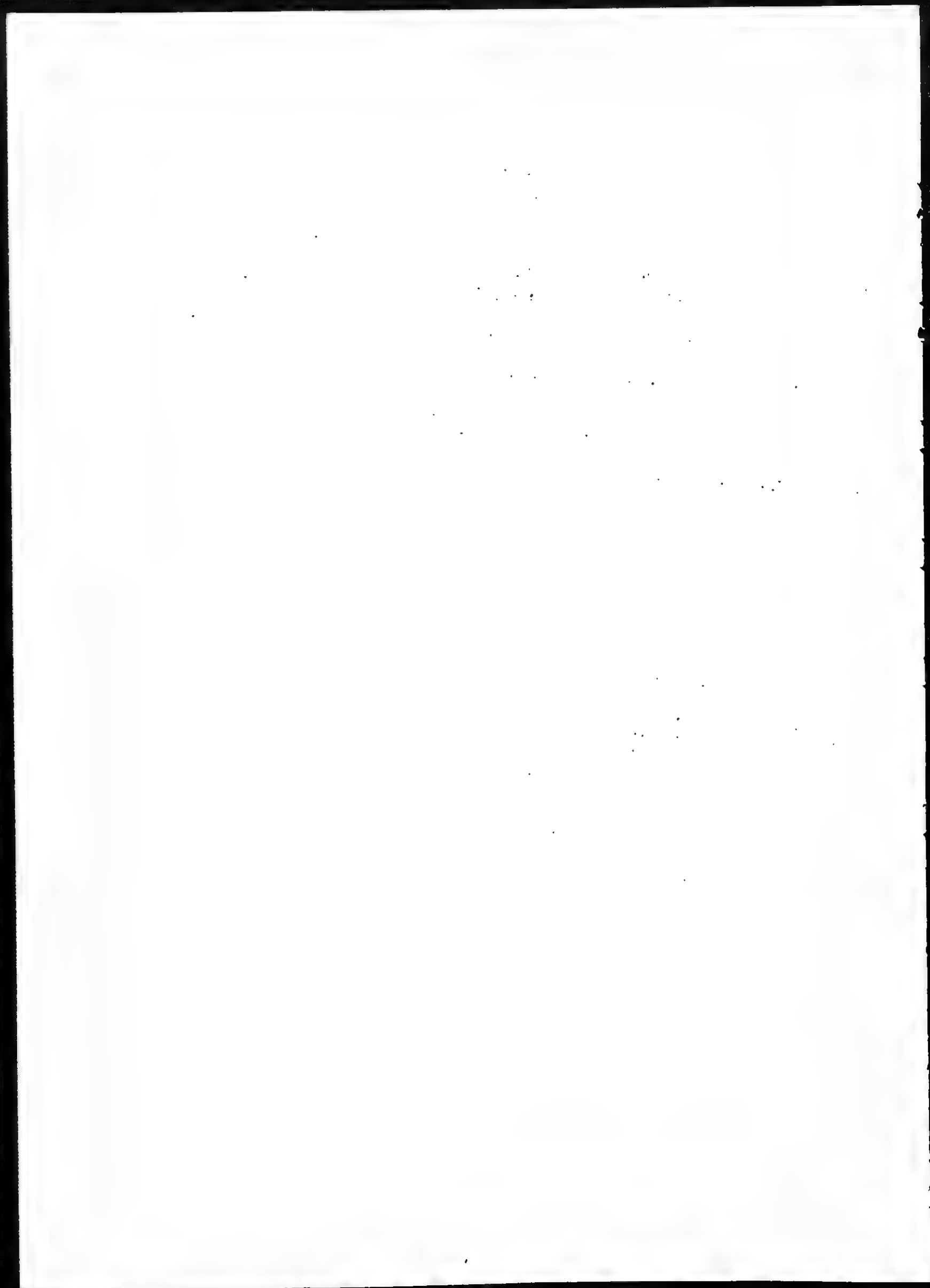
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### JURISDICTIONAL STATEMENT

The jurisdiction of this Court is granted by the Act of March 4, 1913, 37 Stat. 989, ch. 150, § 8, par. 65, as amended by Act of August 27, 1935, 49 Stat. 882, ch. 742, § 2; District of Columbia Code, 1951, Title 43, Section 705. Section 705 directs the District Court in adjudicating an appeal from an order of the Public Utilities Commission of the District of Columbia either to dismiss the said appeal and affirm the order of the Commission or sustain the appeal and vacate the Commission's order. In either event," any party, including said Commission, may appeal from the order or decree of said court to the United States Court of Appeals for the District of Columbia which shall thereupon have and take jurisdiction in every such appeal. "

The Order of the District Court dismissing appellants' appeal and affirming the Order of the Commission is set forth at pages 38-41 of the Joint Appendix. The Notice of Appeal appears at page 42 of the Joint Appendix.

The scope of the Court's review is set forth in Title 43, Section 706 of the District of Columbia Code, 1951.

### STATEMENT OF THE CASE

On November 6, 1959, appellee Transit filed with appellee Commission a petition for a change in its schedule of rates to be charged in the District of Columbia. By Order No. 4585, dated November 9, 1959, the Commission suspended the proposed schedule of rates for a period of 120 days and ordered an investigation and public hearing of the subject matter of Transit's petition.

The Commission granted appellant Goodman leave to intervene as one of six public petitioners. Appellant Goodman participated actively in all phases of the Commission's investigation appearing as attorney pro se, as counsel for intervenor Friendship Citizens Association and as co-counsel for the individual public petitioners. On January 25, 1960, appellant Bebchick entered his appearance as co-counsel for the public petitioners. In representing their respective interests, appellants cross-examined the witnesses of the Commission and Transit and sponsored two expert witnesses--an economist and an accountant specializing in transportation matters--who testified in detail and introduced numerous economic exhibits and studies relating to the rate of return, rate base, operating expenses, and other matters relative to the fare proposal under investigation.

After the conclusion of the extensive hearings, the Commission issued its Order No. 4631, dated March 2, 1960

(hereinafter the "Order") finding that an increase in the cash fare charged by Transit in the District of Columbia from 20¢ to 25¢ was reasonable (JA 1). Immediately upon the issuance of the Commission's order, Transit filed a tariff embodying such an increase, which became effective March 6, 1960. On March 31, 1960, the Commission issued an Opinion in Support of Order No. 4631 (JA 5) (hereinafter the "Opinion").

On April 1, 1960, appellants Bebachick and Goodman, among others, duly filed a Petition for Reconsideration of the Commission's Order. By Order No. 4645, dated April 27, 1960, the Commission denied all relief prayed for in this petition for reconsideration.

Whereupon appellants, with three other individual transit riders, filed a petition of appeal with the United States District Court for the District of Columbia (C.A. 1529-60) pursuant to Title 43, Section 705 of the District of Columbia Code (JA 32). As appears in the docket entries (JA 30-31), defendant Transit filed a counterclaim (more properly denominated a cross claim against the Commission). Thereupon appellants and Transit moved for summary judgment and the Commission moved to dismiss.

On September 15, 1960, the District Court, per Judge Letts, dismissed appellants' Complaint on the grounds that they lacked standing to sue as there was no evidence in the record made before the Commission to establish that they were transit

riders. Thereupon, this Court, on appeal of appellants Bebachick and Goodman reversed the order of the District Court and remanded the case for a hearing on the merits. Bebchick, et al. v. Public Utilities Commission, 109 U.S. App. D. C. 298, 287 F. 2d 337 (1961).

On remand, the parties stipulated to the dismissal of Transit's counterclaim; and after various mesne motions and orders, the Court, per Judge Walsh, denied appellants' motion for summary judgment, granted the Commission's motion to dismiss and affirmed the Commission's Order (JA 39). Thereafter appellants filed their Notice of Appeal (JA 42).

#### STATUTES INVOLVED

This appeal involves, in part, the construction of sections 4, 7, and 9 of Transit's Franchise Act of July 24, 1956, Ch. 669, 70 Stat. 598. The sections are set forth in Appendix A hereto.

#### STATEMENT OF POINTS

1. The Commission erred in concluding that Transit was entitled to an increase in the cash fare charged in the District of Columbia from 20¢ to 25¢ and in issuing an Order which has the end result of burdening transit riders with arbitrary and unreasonable revenue deductions, of allowing Transit excessive earnings and in permitting a cash fare 25% higher than the national median or average transit fare.

2. The Commission erred in permitting any further accrual for future contingent track removal and repaving costs and particularly in allowing the excessive amount of \$1,044,196 as the accrual for the future annual period.

3. The Commission erred in allowing depreciation, at normal rates, on (a) approximately \$2.5 million of abandoned street rail properties, and (b) approximately \$2.5 million of street rail properties currently in service.

4. The Commission erred in allowing in addition to normal rates of depreciation on abandoned street rail properties, a special amortization allowance of \$295,000 annually to provide for the complete recovery of the remaining undepreciated cost of these abandoned properties.

5. The Commission erred in allowing depreciation of approximately \$250,000 on buses which already have been fully depreciated.

6. The Commission erred (a) in maintaining a bus depreciation policy which permits the accrual of depreciation on fully depreciated buses and which has resulted in the accrual of approximately \$1,200,000 of excess depreciation, and (b) in refusing to modify the existing method of bus depreciation so as to permit depreciation on buses to be accrued at a rate and over a service life of which the Commission already determined to be proper.

7. The Commission erred in finding or concluding that a return of \$660,146 for the future annual period was below the range of a fair and reasonable return.



8. The Commission erred in finding or concluding that a return of \$1,143,249 falls within the range of a fair return.

9. The Commission erred in failing to adhere to or to properly apply the capital attraction standard of Transit's Franchise in determining the fair return which Transit may be permitted to earn.

10. The Commission erred in failing to limit Transit's rate base to Transit's prudent investment in assets devoted to the public service.

11. The Commission erred in adopting a system rate base of over \$16 millions and in failing to adopt a rate base not exceeding the purchase price value of Transit's properties used and useful in the public service.

12. The Commission erred in increasing Transit's rate base to include (a) Transit's contingent liability for conversion to an all-bus operation, (b) amortized portions of the acquisition adjustment, and (c) the reserve for track removal and repaving.

13. The Commission erred in adopting a rate base which contains approximately \$2.5 million of abandoned rail properties for the obsolescence of which Transit's investors already have been fully compensated.

14. The Commission erred in adopting a rate base at a level which effectively includes amounts contributed by the transit riders through operating expense charges.



15. The Commission erred to the extent it concluded that it was relying upon gross operating revenues as the rate-making standard to determine Transit's fair return.

16. The Commission erred to the extent that it found or concluded that "conditions warrant" a shift to the gross operating revenues standard of determining fair return, as those terms are used in Section 4 of Transit's Franchise; the Commission erred to the extent that it relied upon ex parte communications and an immature determination regarding the circumstances warranting use of a revenue method.

17. The Commission erred in limiting examination, in failing to take cognizance of, and giving appropriate weight to, Transit's failure to make economical and efficient use of its cash resources, and Transit's banking policies.

18. The Commission erred in failing to take cognizance of and giving appropriate weight to the sale of stock in the parent company of Transit by the grandparent company to obtain windfall capital gains.

#### SUMMARY OF THE ARGUMENT

The end result of the Commission's Order permitting Transit to increase its cash fare from 20¢ to 25¢ is an unreasonably high and unlawful fare level for the District of Columbia. The increase results in burdening the farepayers with revenue deductions, depreciation, and other accruals which are excessive and improper. Transit is permitted to realize a return on its

investment far in excess of its requirements to attract capital on favorable terms, a return which is measured against a swollen rate base exceeding the company's prudent investment.

This appeal presents the decline of responsible regulation by a Commission which relies at every turn upon unsupported judgment and has acted contrary to clearly enunciated standards of law.

1. The Commission unlawfully permits Transit to annually accrue more than one million dollars over a ten-year period to cover the future contingent costs of track removal and repaving. Transit purchased its assets for \$10 million less than their book value in contemplation of the expenses involved in the conversion program. Moreover, Transit currently has book reserves sufficient to cover the expenses of track removal of which over \$3 million was obtained through accruals from the farepayers and there is no justification in further burdening transit riders with this contingent expense.

Furthermore, any further accruals for track removal unreasonable in light of the evidence that Transit has expended less than 1% of the more than \$3 million already accrued for this specific purpose, and that no testimony was offered as to what track removal expenses would be incurred either in the future annual period utilized by the Commission in this proceeding as the period for determining rates or in any future period. Indeed, it now appears that by fiscal 1966, the end of the ten-year accrual period, Transit will have expended

only \$3 millions (even before reductions to reflect applicable income tax benefits) for such a removal program.

Finally, the annual accrual is based upon an estimate that the total program of complete track removal and repaving would cost Transit some \$10.5 millions. But that estimate may not properly be used since it is based on the assumptions (a) that Transit would pay all expenses by itself and (b) that there would be a complete removal program. These assumptions are contrary to fact: First, the law requires the District of Columbia to share substantial costs of street repaving when tracks are removed. Second, Transit in many instances has been and is permitted by the Commission to pursue the less expensive course of merely asphaltting over trackage rather than removing it.

2. The Commission unlawfully permits Transit to accrue depreciation with respect to more than \$2.5 million of street rail properties which have been abandoned and are no longer used and useful in the public service. Transit has been accorded both (a) depreciation on these abandoned properties at normal rates, and (b) in addition, a special annual allowance of \$295,000 to insure the complete depreciation of these abandoned properties.

There is no justification for allowing further depreciation on any street rail properties, particularly those which have been abandoned.

When Transit purchased the assets of the predecessor company, it was on condition that the street rail properties would be abandoned within seven years as part of the conversion to an all-bus operation; in contemplation of this assumed contingent liability, Transit received a \$10 million discount from the book value of all properties acquired. Only when and to the extent that Transit invests any such additional sums may such amounts be used as the basis for calculating depreciation accrual or annual return. Moreover, Transit has received extremely high earnings and paid large dividends since the formation of the company. To the extent Transit's investors assumed any "risk of obsolescence" of the rail properties, they have been fully compensated and there is no warrant for allowing a continuing charge based on abandoned properties.

3. The Commission continues to permit Transit to accrue depreciation on more than 300 buses which already have been fully depreciated, and which has resulted in an accrual of over \$1.2 millions to date beyond the original cost of those buses. The Commission ignored the substantial evidence of record and erred in failing to end the illegality of double-charging transit riders for depreciation on fully depreciated buses.

4. The Commission erred in finding that a net return to Transit of \$660,000 under the existing 20¢ cash fare was an insufficient return, and that a return of \$1,143,249 resulting from the increased cash fare would constitute a fair

return. This fare increase permits Transit to maintain a 100% dividend on the investment in capital stock and to continue the accumulation of large additional amounts as earned surplus. All told the fares provided by the Commission yield a return (after interest and taxes) as high as 30% on total equity (capital stock investment in 1956 plus the earned surpluses accumulated between 1956 and 1960 over and above dividends).

In allowing this excessive return, the Commission relied solely upon unsupported judgment and failed to make those basic findings requisite for rate-making proceedings.

5. The Commission erred in adopting a rate base which is in excess of Transit's prudent investment in used and useful transit properties. This excess results from two unlawful additions made by the Commission. (a) It added a substantial amount to take account of the fact that the original cost of the assets to Transit's predecessor was a higher figure, a factor which does not entitle Transit to a higher return than its own prudent investment. (b) It added a substantial amount because of Transit's contingent liability to convert to an all-bus operation, a factor which entitles Transit to an additional return only when, as, if, and to the extent that such liability actually results in additional investment by Transit.

The Commission improperly increased the rate base above Transit's purchase price through the device of including in

the rate base part of the acquisition adjustment (the difference between Transit's purchase price and the higher original cost to Transit's predecessor). The inclusion in the rate base of part of this adjustment, over and above Transit's purchase price, was improper in and of itself and also contrary to the Commission's handling of annual depreciation charges, where the depreciation base of original cost to the predecessor was reduced by the write-off of the acquisition adjustment so as to insure that annual depreciation charges would not recoup to Transit an amount greater than its purchase price.

The courts and regulatory agencies have clearly held that the purchase price of properties may not be distorted by acquisition adjustments where, as in the present case the acquisition occurred at arm's length and the difference between the seller's cost and his price was not fictitious.

Similarly, there is no warrant for including in the rate base funds already collected from the public for track removal and repaving.

The crux of the matter is that while the amounts represented by the acquisition adjustment and the track removal reserve may represent an assumed obligation by Transit, this remains a cost-free obligation--free of the service of debt or the need to pay dividends--until Transit devotes additional capital to the enterprise on account of such obligation.



6. The Commission's valuation of a \$16 million rate base is erroneous and unlawful. The Commission's own staff witness testified that the only proper rate base valuation was one based on purchase price. Further, a sizable portion of the Commission's \$16 million average rate base contains amounts which already have been contributed by transit riders as operating expenses. It is elemental that farepayers may not be double-charged and required to provide a utility with a return on funds which they have contributed through the payment of operating expenses.

This adjustment for excessive operating reserves would reduce the so-called purchase price rate base to a figure reflecting the total capital investment made by Transit's creditors and stockholders (including retained earnings), and would conform to accepted principles for ascertainment of appropriate rate base.

Finally, the Commission erred in including in the rate base some \$2.5 millions of abandoned street rail properties not used and useful in the public service.

7. The Commission's order derives no support from its reference to a gross operating revenues method of rate-making. The Commission properly rejected Transit's contention that gross operating revenues should determine the basis for fixing rates, and it actually used the traditional rate base-rate of return standard as the ultimate test of reasonableness of the return element. At best, gross operating revenues was

utilized as a rough means of verifying a result reached by the traditional method; it was not sufficient to constitute an independent ground of decision.

The governing statutory provisions clearly contemplate the ultimate and traditional capital attraction standard, a standard that does not vary regardless of the technique employed in determining fair return. The Commission could depart from the rate base- rate of return on investment standard only upon a finding that the capital needs of the company so necessitated. No such finding was made by the Commission nor would the evidence support such a finding.

The Commission's reference to Transit's conversion program as constituting "conditions" "warranting" a shift to gross operating revenues did not constitute such a finding. Moreover, such a reference was improper as the Commission there relied upon ex parte communications and an immature prior declaration of the Commission, not the subject of hearing, which the District Court has held not to be a final order.

8. The Commission erred in failing to take account and give proper weight to the sale of stock in the parent company of Transit by its grandparent company to obtain windfall capital gains. This evidence directly affects a central issue in the case--Transit's ability to attract capital on favorable terms. More specifically, it is relevant in determining to what extent any future need for increased earnings or any future inability or disability in raising capital results from the improper



and unjustified activities of management--a risk against which the farepayers should not be required to provide relief.

The Commission further erred in limiting examination as to Transit's policy of maintaining cash deposits of approximately \$1.5 million in non-interest bearing accounts in New York banks which deal with Transit's grandparent airline company. There is no warrant in using funds contributed by Transit riders in such a fashion from which they derive no benefit. Transit's income should be debited with constructive interest in an amount equal to that which such funds might have earned if invested in short-term government securities.

## ARGUMENT

### I

THE COMMISSION HAS UNREASONABLY AND UNLAWFULLY PERMITTED TRANSIT TO EARN LARGER REVENUES THAN NEEDED TO ATTRACT CAPITAL, RECOUP INVESTMENT, PAY OPERATING EXPENSES, AND PROVIDE THE SERVICE, AND HAS THEREFORE BURDENED DISTRICT CONSUMERS WITH UNLAWFULLY HIGH FARES.

The end result of the Commission's Order and Opinion in this proceeding--a 25¢ cash fare--represents an unreasonably high and unlawful fare level for the District of Columbia. At every turn throughout its determination of the case the Commission has systematically allowed D. C. Transit opportunities to earn excessive income, virtually abandoning the consumers, its most sacred charge.

The fares have been burdened with unfair and unreasonable revenue deductions, including excessive depreciation and excessive accruals to the reserve for track removal and repaving (Section II, infra). Allowable earnings, in turn, have been measured against a swollen rate base greatly in excess of the company's prudent investment and containing certain abandoned properties (Sections V and VI, infra). Transit thereby has been allowed the opportunity to earn excessive operating income--i.e. net earnings greatly in excess of its requirements to attract capital on favorable terms after covering operating expenses--revenues which constitute a 30% return on Transit's total equity investment (JA 25) and which have permitted the Company to annually pay its stockholders dividends at the present rate of 100% of their present capital stock investment (JA 24, 65, 117-119). Sections III and IV, infra). With such excessive

fares the Company has paid off millions of dollars of short-term debt obligations (JA 115-116); and has become so affluent that it has removed several millions of dollars contributed by District transit riders from the public service and stored such funds in non-interest bearing bank accounts in institutions, outside the District of Columbia, which provide financing to Transit's grandparent company, Transportation Corporation of America, d/b/a/ Trans Caribbean Airways (Section VIII, infra).

The end result of the Commission's action has been to impose on District transit riders a cash fare of 25¢, made effective in the District on March 6, 1960, which is 25% higher than the average fare in effect in the thirty largest cities of this nation. Both the national average transit fare and the national median transit fare (cash or token) is only 20¢ (JA 50).

The unreasonableness and lack of justification for the Commission's allowance of a fare increase in this proceeding is underscored by the national trend of declining transit patronage, the automobile traffic dilemma of the District of Columbia, and the interest of both the public and Transit in keeping the fares at the lowest level consonant with the preservation of the company. See Spiegel v. Public Utilities Commission, 96 U.S. App. D.C. 307, 226 F.2d 29, 31 (1955), cert. denied 350 U.S. 904 (1955). In permitting such a result the Commission has persistently ignored governing legal

principles enounced by this Court. This case marks a collapse of responsible regulation with the agency seeking to obviate review and criticism with a cloak of unsupported "judgment". This appeal involves not only an unreasonably high 25¢ fare but also the propriety of the rate-making process in the District of Columbia and the adherence to governing standards of law.

## II.

### THE COMMISSION ALLOWED TRANSIT ARBITRARY AND UNREASONABLE OPERATING EXPENSES

The Commission erred in finding and concluding that net operating income of \$660,146 would result from the fares in effect prior to March 6, 1960, and \$1,143,249 from a 25¢ cash fare. Both amounts were determined after allowances of excessive operating expenses, which improperly burdens the fare-payers.

1. The Commission Erred In Its Allowances Of Accruals For Track Removal and Repaving.

The Commission erred in allowing Transit as an expense deduction over \$1 million for track removal and repaving which was justified neither by experience nor prophecy in this proceeding. In American Overseas Airlines v. Civil Aeronautics Board, 103 U.S. App. D.C. 41, 254 F.2d 744, 750 (1958), this Court clearly stated that it would be improper for a commission "to cushion a company in advance against unforeseen events which are not ordinary or necessary in the sense that ordinary and necessary expenses are forecast in a prospective rate case."

See also City of Detroit, Michigan v. Federal Power Commission, 97 U.S. App. D.C. 260, 230 F.2d 810, 817 (1955), cert. denied 352 U.S. 829 (1956).

In the first place, no expense allowance whatever is warranted for track removal and repaving. This program of removing the entire network of streetcar tracks and repaving the street surface is a burden assumed by the investors in Transit under section 7 of the Franchise, and in no sense is an operating expense of the company. This program does not involve the ordinary expense of maintenance of the track facilities, but on the contrary involves the "complete removal of the entire track structure" (JA 13), a requirement imposed by law in order to obtain a franchise in the District of Columbia.<sup>1/</sup> Moreover, it is unreasonable and unlawful to require the fare-payers to make contributions of capital to Transit by the device of an allowance for track removal and repaving.

The substantial evidence is that Transit's purchase price was as low as it was (discounted by over \$10 million below the book values of the properties) by reason of the assumed liability for track removal and repaving. Transit argued in 1957 that the full \$10 millions should be set up as a reserve to cover future track removal (JA 83-84); and Transit's witness Flanagan testified in a proceeding in 1958 that the consideration

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<sup>1/</sup> A seven-year program for converting the streetcar operation to an all-bus operation was formulated by the District as early as 1955. Indeed, the District Commissioners' insistence that a new operator begin immediately in 1956 with an all-bus operation dissuaded many from bidding for the franchise. The history of this matter is summarized by Congressman Harris in 102 Cong. Rec. 8289, May 16, 1956.

given by Transit's investors for the properties, besides cash and securities, included also "the obligation . . . to convert from streetcar operation to bus operation, to remove the streetcar tracks, and to repave the track area" (JA 68; see also JA 128-129). Witness Falk of the Commission's staff testified that the additional cost of track removal was the reason why the predecessor company was "willing to sell the company at the figure it did". (JA 142). As witness Harris stated, Transit received an involuntary contribution or donation of assets (JA 218-221). When and if Transit's investors should bring into the company whatever additional capital may be required to discharge their obligation for track removal and repaving, then and only then should they be permitted to recover these amounts from the farepayers through annual charges and to receive a return on such monies.

In any event, the Commission's allowance of \$1,044,196 on this record is excessive and unlawful. The witness for the company was asked on cross-examination whether he had any estimate of the track removal and repaving expense which the company would incur in 1960 (the future annual period); he replied, "No" (JA 249). He was asked whether he could estimate how much would be spent for this purpose in any specific future period; he replied: "The answer is no; I cannot." (JA 250). There was a complete failure of proof on the part of the company to justify any allowance in the future period for track removal and repaving.



The past experience of the company in removing tracks and repaving further justified only a nominal allowance in the future period, if any. As of the beginning of the future period, Transit had already accrued a reserve of \$3,216,286 (JA 49). Yet, in 1958 Transit expended only \$12,735 after salvage, and in 1959 only \$48,602 (JA 183). Thus, the actual facts are that in a period of more than one-third of the ten-year accrual period, the amount that Transit has actually been required to spend amounts to only 1/2 of 1% of the purported total cost of track removal.

The unreasonableness of this expense deduction in the present record is confirmed by the fact, revealed in a subsequent rate proceeding before the Commission, that the total cost to Transit of all contemplated track removal and repaving projects through fiscal 1966 (the end of the ten-year accrual period) would be approximately \$3,000,000, and no greater than \$3,500,000 even assuming unforeseen contingencies such as subway construction. As of September 30, 1960, Transit had already accrued unexpended track removal funds in excess of \$4,000,000. The Commission in that opinion concedes that the contemplated expenditures through fiscal 1966 would change appreciably only when and if the Commission itself ordered a departure from existing policy and an acceleration of the



contemplated conversion program.<sup>2/</sup>

Not only is any further build-up in the reserve for track removal and repaving unwarranted in light of reasonably foreseeable costs and needs, but the entire basis for the accrual approved by the Commission rests on fallacious assumptions which invalidate its propriety.

Transit is permitted by the Commission to accrue \$1,044,000 annually for a period of ten years to provide it with a total amount of \$10,440,000, the total gross cost supposedly involved (without any adjustment for the partial tax offset) in the track conversion program (JA 13). But the \$10,440,000 figure is a hypothetical estimate of the total cost of a removal program without regard to the parties involved in its implementation. It would be Transit's cost only if Transit were by itself required to remove all the tracks and repave the former track area and bear the entire cost thereof (JA 13). But this is not the case.

Section 7 of the Franchise requires that Transit and the District of Columbia Highway Department, to the fullest extent

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<sup>2/</sup> Re. D. C. Transit System, Inc., 38 PUR 3d 19 at 43, (DCPUC, Opinion in Support of Order No. 3640, February 27, 1961).

In this proceeding the Commission rejected an increase sought by Transit in its fare from 5 tokens for \$1.00 to 4 tokens for \$0.95. Appellant Bebachick has appealed this Order to the U. S. District Court for the District of Columbia (C.A. 825-61), where it currently is pending, on the grounds that the Commission erred to the extent that it found the existing \$0.25 cash fare to be reasonable and in failing to find and order a reduction in the cash fare of \$0.25 given the evidence of record.

possible, integrate the track conversion program with the District's street maintenance and improvement program.

As a matter of law, Transit and the District of Columbia share the costs of repaving street areas from which track has been removed wherever the track conversion and highway maintenance programs are so integrated. Section 7 of the Franchise and D. C. Appropriation Act, 1942, 55 Stat. 499, 533.

Moreover, in effectively implementing the policy of Section 7, the Commission has granted its requisite approval in many cases to a program whereby Transit has been permitted in many cases to merely "recap" its abandoned trackage (cover them over with asphalt without removing them), rather than undertaking to remove the tracks and then repave the areas torn up in the process.<sup>3/</sup> The cost of recapping is but a small fraction of that involved in the removal process.

Thus, the current accrual is based on assumptions as to the nature of the track conversion program and to the costs to be borne by Transit which are simply contrary to fact. This, by itself, renders the current accrual invalid.

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<sup>3/</sup> The Commission contends that Transit bears the legal responsibility of removing all trackage, and thus would be responsible for the costs involved if it were required at some future time to remove that portion of the trackage now being recapped (See 38 PUR 3d 19 at 43 (1961)). But there are no plans for the removal of such recapped trackage; nor is there any indication that such a need ever will arise.

Surely the transit riders cannot be compelled to prepay Transit for such highly contingent costs of an indeterminate amount which Transit may never incur, and if so, at some distant future date.

2. The Commission Erred in Allowing  
Unlawful Depreciation.

The Commission erred in allowing any or excessive depreciation on rail properties, particularly abandoned rail properties, and in allowing depreciation on fully depreciated buses.

a. Depreciation of Rail Properties.

(1) Abandoned Properties. In this proceeding, the depreciation on rail properties includes over \$460,000 depreciation at normal rates on abandoned rail properties.<sup>4/</sup> A full 49.4% of Transit's rail properties were abandoned and were no longer used and useful in the public service at the start of the future annual period, but nevertheless were included in the rate base (JA 52; 142-143). The Commission compounds the evil; not only does it require the ratepayers to provide depreciation on abandoned rail properties but it requires the annual charges to be increased above normal depreciation rates by ordering the Company to accrue a further special amortization allowance of \$295,000 annually (JA 14-15, 52). The Commission did this so that the rail properties already abandoned will be covered by depreciation deductions by mid-1963, the time by which the Commission believes Transit will

<sup>4/</sup> This \$460,000 is 49.4% of the \$933,569 "normal" depreciation taken by Transit, i.e. the figure established in 1953, for depreciation for all rail properties, based on Capital Transit's original cost (JA 14, 52, 230; see 1953 order at JA 73). As will be pointed out below, see Section V.2., *infra*, this depreciation reserve is reduced by a credit for "amortization of the acquisition adjustment" to approximate a depreciation based on purchase price paid by Transit for all properties. This reduction does not affect the validity of the point here discussed, that Transit is receiving substantial current depreciation on the basis of rail properties already abandoned.

have completed its program of converting from streetcars to buses. To repeat, transit riders through the fares are providing depreciation at normal rates for all street rail properties (half of which are abandoned) and in addition a special allowance for the abandoned properties. (See, e.g. JA 52)

The law concerning the allowance of depreciation on abandoned properties, like that of including such abandoned properties in the rate base, is hardly novel in this jurisdiction. This Court made it emphatically clear that neither depreciation nor inclusion in the rate base of such properties was lawful unless the Commission specifically found that the investor had not been recompensed for the risk of obsolescence. Washington Gas Light Co. v. Baker, 88 U.S. App. D.C. 115, 188 F.2d 11 (1950), cert. denied, 340 U.S. 952 (1951). The conversion requirement was a condition of the grant of Transit's Franchise and the low price (below book value) it paid for the properties reflected this assumed liability. As described infra (Section VI 3) Transit's investors have been recompensed many times over for the problem of obsolescence.

The Commission here has failed to make the type of finding which this Court has directed be made as a condition precedent to permitting depreciation and a return on abandoned property. And no such finding could lawfully have been made in view of the overwhelming and substantial evidence of record --which is perhaps why the Commission bypassed the subject in its findings.

(2) Rail Properties Generally. Moreover, the acquisition adjustment and the reserve for track removal are both reserves (JA 176-179). They are today adequate to cover not only the net cost (after salvage and tax offsets) of all track removal and repaving; but in addition the total cost, not previously recovered through depreciation reserves, of all rail properties--streetcars abandoned as well as streetcars still in use and slated to be converted.<sup>5/</sup> The Commission may not lawfully ignore these other reserves on the books, and is required to assure they will be used for the benefit of the farepayers to cover any outstanding liabilities for retirement of streetcars as well as for track removal and repaving.

On the present record, the farepayer is also entitled to avoid any further depreciation on streetcar properties (JA 70-71, 176-179), and to insist that only an added annual accrual of some \$184,000 is needed to provide for the cost of all track removal and repaving (over \$10 millions) that the Commission believes will be incurred at some future date assuming the consumer must bear this expense. (See also JA 209, et. seq.)

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<sup>5/</sup> Witness Harris testified that present book reserves are sufficient to provide for the retirement of all rail properties and for all conversion costs with the exception of a small annual charge of about \$184,000. (JA 15-16, 67, 70, 71, 226).

It may be noted in passing that even if the Commission had properly determined that the farepayers should bear the burden of this expense, it erred in allowing Transit to accrue this expense on the basis of the gross cost of removing tracks and repaving. Obviously if the farepayers are to bear this burden, then they should also obtain the advantage of the reduction in income taxes resulting from such expense. Hence, as witness Harris developed, no more than 46% of the gross cost need be reserved, for the remainder will be saved through reduction of future taxes. Ibid, and JA 180, 181-182.



b. Depreciation of Bus Properties.

The allowance for bus depreciation is excessive and unlawful. Pursuant to the foregoing 1953 study, the company was allowed to accrue depreciation at a flat rate of 7% of the original cost of the bus properties to the owner first devoting the property to the public service. The particular percentage was chosen in order to depreciate bus properties over a 14-year life (JA 74). However, the Commission's present practice, as admitted by its own witness, permits the company to accrue more than the depreciation prescribed in 1953, and hence to violate its own order. See, e.g., JA 237.

The Commission has directed the Company to utilize a "group method" of bus depreciation. Under this method, all the bus properties are depreciated as a group, and a flat percentage of the original cost of all buses in the group is allowed as annual depreciation. Under the Commission's practice, buses are not removed from the group until they are actually retired from service.

As a matter of actual fact and experience, the age of over 400 buses at the beginning of the future period were greater than 14 years (JA 47, 120). Since the rate of group depreciation is based on a 14-year life, this results in a depreciation allowance for buses already fully depreciated. As of September 30, 1959, the depreciation reserve built up in this way included over \$1,200,000 of excess depreciation that had been accrued over and above the entire cost of those buses,

i.e. accrued on buses that had already been fully depreciated (JA 15, 120).

During the test period, the Commission permits Transit to accrue \$246,253 during the future annual period for the further depreciation of well over 300 fully depreciated buses, some of which are over 20 years of age (JA 70, 71, 214-215).

The evidence of record clearly indicates that there is no justification for this policy of double-charging the farepayers for depreciation on fully depreciated buses. While buses remain in the depreciable group in excess of 14 years, almost none are retired from service prior to 14 years. The Company's witness Flanagan testified that Transit never retires buses prior to 14 years unless accidentally wrecked (JA 247), and the Commission's witness Falk testified that such early retirements were "very minor" and were not appreciable (JA 236-237). Thus, depreciation of fully depreciated buses is not counterbalanced by premature retirements of buses, and this fact is reflected by the excess depreciation of \$1,200,000 already collected. Nor was there any evidence introduced which in any way would indicate that the Company will in the future be retiring buses prior to 14 years; indeed there was evidence the company had no such plans (JA 247). It is not denied that the bus reserves are already over-accrued and that they will continue to over-accrue. See JA 119-120, 237.

The Commission disingenuously suggests that this injustice to the farepayers is an unavoidable concomitant of the "group" method. This is utterly indefensible. If the Commission had



properly defined the group, and established proper depreciation rates (i.e., below 7% per annum) this injustice would not have occurred. The Commission was under an obligation to take some proper corrective action at this time, and its failure to do so is error. The Commission admits that the "group" life should approximate the actual average experienced service life of buses (JA 17).<sup>6/</sup> The Company's record clearly indicates the dates upon which various buses were placed in the group in service and made part of the group. (JA 47). As witness Harris proposed, the solution is merely to remove from the depreciable group those buses which are more than 14 years of age and in the future to remove buses as they reach 14 years of service (JA 184). In this manner, the ratepayers would be assured of providing for only such depreciation which the Commission itself has deemed to be just and proper.

The Commission maintains that any change in the depreciation allowed the company must await a new depreciation study (JA 18). But, the Commission reaches an unlawful end result with its present method, which, therefore, cannot be sustained on this appeal.

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<sup>6/</sup> Indeed, other administrative agencies expressly require a group method of depreciation to be based on the average of the actually experienced service lives of property. The Interstate Commerce Commission requires group depreciation to be "determined from the average of the service lives of all property" in the account (49 CFR 182.01-23). The Civil Aeronautics Board allows overhaul reserves for engines on a unit or group basis, but in any event, "based on representative experienced and anticipated overhaul costs per hour flown. . . ." (14 CFR 241.5-4(g)(6)).

And in a subsequent rate case, the Commission determined that buses should be depreciated on a unit basis over 17 years.<sup>7/</sup> The problem in this proceeding, however, is to keep the depreciation allowance for buses at least within the level prescribed in 1953. The subsequent recognition by the Commission of Appellants' position hardly cures the error here committed.

The Commission errs as a matter of law in double-charging the farepayers for depreciation on fully depreciated buses, thereby allowing Transit far more than needed to maintain the integrity of its investment. Cf. Lindheimer v. Illinois Telephone Co., 292 U.S. 151, 167 (1934).

### III

THE COMMISSION'S ALLOWED EARNINGS OF \$1,143,249 IS UNSUPPORTED BY FINDINGS OR EVIDENCE. FURTHERMORE THE EVIDENCE OF RECORD DOES NOT JUSTIFY A RETURN IN EXCESS OF \$660,000.

The Commission's "Determination of Fair Return" in the Opinion in Support (JA 23-27) proceeds in the following vein:

1. Where "operating ratio" method is used, according to the Commission's staff witness, there is "no formula or method" for determining an appropriate return on revenues and the return to the company above expenses "seems to be a matter of the exercise of the rate-making authority's best judgment in the light of the facts in the particular case being considered." (JA 24);
2. Witness Falk testified and we agree that "a fair return should provide sufficient income, over

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<sup>7/</sup> See 38 PUR 3d 19 at 34 (1961). The Commission erred, however, in establishing a unit method of depreciation and a 17-year life for only 6 months of the annual test period with the result that the revenues continue to reflect doubled charges.

and above all expenses, to meet interest requirements on debt capital, allow the payment of reasonable dividends, and, in addition, permit the retention of some portion of earnings in surplus." (JA 24, see also JA 27);

3. Earnings under present fares will amount to \$660,146, which is equivalent to a return of 2.47 percent of revenues or 4.12 percent on a rate base of \$16,016,810 (JA 24);
4. "Witness Falk testified that interest charges during 1960 would be approximately \$317,000 and if dividends are maintained at the current level another \$500,000 will be required. It was witness Falk's opinion that without some increase in rates the requirements of a fair return will not be met. In our opinion a return equivalent to 2.47% on gross operating revenues or 4.12% on rate base is below the range of a fair and reasonable return."  
(JA 24);
5. The fare structure proposed by the staff will result in income of \$1,143,249 [assuming the increase is effective for 10 months of the future period]. "In the opinion of the staff witness, net operating income at this level would constitute a fair return. Under the standards which we have heretofore adopted we conclude that a return of \$1,143,249 falls within the range of what we consider to be a fair return." (JA 24-25);
6. "Witness Falk testified that such a return on equity capital [30 percent] would fall within the range of a reasonable return when consideration is given to the relatively low percentage of equity capital invested in the business and to the element of risk inherent in any investment in the transit industry. With this the Commission agrees." (JA 25);
7. A reasonable return "calls for the exercise of sound judgment and common sense" and the average of ratios allowed in other jurisdictions does not necessarily constitute a fair measure of Transit's needs. (JA 27);
8. "Based on all the foregoing, the Commission concludes that net operating income of \$1,143,249. . .

will provide the Company with a fair rate of return as measured on either the gross operating revenues method or the 'rate base- rate of return' method of rate making." (JA 27).

We have set forth the Commission's discussion at some length, for we believe that it reveals the lack of those basic findings which this Court has stated must accompany the ultimate finding of fair rate of return. See Capital Transit Company v. Public Utilities Commission, 93 U.S. App. D.C. 194, 213 F.2d 176, 186 (1953). The Commission computes the earnings that will result under the various fare structures; then states whether or not in its judgment such earnings are reasonable. It never independently determines what earnings are needed, but only what earnings will result. Nowhere does the Commission set forth how it reaches the conclusion that Transit "needs" earnings of \$1,143,249 to make it an attractive investment to private investors, as required by section 4 of the Franchise. There is no determination, or standard for determining, that present annual dividends of \$500,000 (or 100% of the present capital stock investment) and an additional \$300,000 for retained earnings--or a return of 30% on the total present equity investment--are needed by Transit to attract capital.<sup>8/</sup>

Pursuant to Bluefield Water Works & Improvement Co. v. Public Service Commission, 262 U.S. 679, 692 (1923),<sup>appellants offered</sup> a comparison with companies of comparable size primarily engaged in transit

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<sup>8/</sup> The only evidence of record is Falk's bare conclusion (JA 133, 134, 145-148). He admittedly included a "cushion" in his recommended return for future, contingent costs divorced from any study of Transit's actual needs (JA 135, 159-160).

operations which had experienced earnings in a representative period. This was expressly disavowed--"the average of ratios allowed in other jurisdictions . . . does not, in our opinion, necessarily constitute a fair measure of the needs of this Company." (JA 27). Yet the Commission did not even begin to outline any other comparison with transit companies to arrive at any specific rate of return.

As this Court has stated before regarding this Commission's determinations of fair return, "Commission expertise alone cannot support so pivotal an assumption." Washington Gas Light Co. v. Baker, 88 U.S. App. D.C. 115, 188 F.2d 11, 16-17 (1950), cert. denied 340 U.S. 952 (1951). "The expertise of a commission usefully serves it in evaluating the evidence, but that expertise cannot supply evidence and cannot, without findings made upon the critical issues before it, guide a commission to a rational and lawful decision." Capital Transit Co. v. Public Utilities Commission, 93 U.S. App. D.C. 194, 213 F.2d 176, 187 (1953).

Throughout the Commission's discussion of the fair rate of return, reliance is placed exclusively on the opinion testimony of witness Falk, the staff accountant. But, this witness made no comparative or individual company study of Transit's return needs (JA 145-148). He testified he had "made no studies of other transit companies . . ." as to fair return (JA 147); and when asked, "And no statistical or analytical studies premise this conclusion of yours" relating to the fair return, he replied "That is correct." (JA 148)



Moreover, witness Falk testified that a return of 7.14% on rate base was fair and reasonable in this proceeding although he had recommended a return of 5.37% on rate base in a prior rate proceeding, and now testified that Transit's risk position had not changed since the prior case (JA 148-149). See Re D. C. Transit System, Inc., 25 PUR 3d 371, (DCPUC Order No. 4480, August 28, 1958).

The staff presentation completely failed to support witness Falk's naked conclusion that a return of \$1,143,249 is fair and reasonable. As this Court stated in the Baker case, supra, "Without any evidence on this essential issue, there is no basis for application of any standard and the judicial review authorized by the statute becomes a formal but futile gesture." The Commission merely lifts itself by its own boot straps by relying upon bare conclusions of its staff witness.

The only study of record of fair return for Transit was presented by witness Limmer in Exhibit 43 (JA 57-60) and related examination. Witness Limmer would allow Transit its interest expense and testified that a return on equity of 12.58% would be fair and reasonable, based on a cost of capital study of Transit in relation to other companies having predominantly local transit operations and average gross revenues

of \$10 millions or more in the 1952-1958 period.<sup>9/</sup>

The Commission improperly gave little weight to the Limmer testimony (See JA 26). The Commission rejected any use of cost of capital method based on earnings-price ratios as a guide to determining a reasonable allowance of return on capital. The Commission stated that such a method is appropriate for gas and electric companies "by reason of their general stability of earnings and dividends, their relative uniformity in capitalization ratios and their large investments in plant per dollar of revenue," but that "this is not the case, however, with respect to transit companies in general." JA 25-26

Significantly, the Commission made no specific comparison of Transit with any other utility, even to determine whether Transit met its theoretical test of a stable company. Also, its reasoning seems inconsistent with the standards for fair return discussed earlier.

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<sup>9/</sup> JA 57-60, 153 et seq., 208-209. All objective indicators of record point to the fact that witness Limmer's recommended return on equity is on the high side of a reasonable range. A return on equity capital of 12.58% provides coverage of fixed charges by four times (JA 60, 158-159, 192-193). The witness used a higher return figure than the one indicated for the Baltimore Transit Company operating in a nearby community of about the same size as Washington. Transit's predecessor had an average earnings-price ratio of 6.70% during the 1952-1954 period and 8.47% 1948-1954; the witness computed a ratio of 11.16% for Transit (JA 58, 171). The current ratio for Transit's parent company, whose only substantial holdings are its stock in Transit is less than 3% (earnings divided by 2,500,000 outstanding shares), indicating that the witness' computed figure is more than ample for the immediate future. (JA 59, 157, 159, 206-207).



In Federal Power Commission v. Hope Nat. Gas Co., 320 U.S. 591 (1944), similar considerations were put forward and overruled. There the Supreme Court held that the return should be sufficient to assure maintenance of credit and attraction of capital, and that such a return is "fair and reasonable" under the Natural Gas Act. This holding was made in spite of Justice Jackson's reflection in dissent that "investment and capacity to serve" as well as investment and profit to be realized, are irrelevant phenomena in the gas industry, "being more erratic and irregular and unpredictable in relation to investment than . . . any other utility business." Id. at 647, 649.

Let us assume arguendo that in a proper case the Commission could reject testimony based on earnings-price ratios as showing actual cost of equity capital. If such testimony and standard--reflecting the dispassionate investors' judgment (JA 205)--is to be rejected, that can only be done if another meaningful standard is employed. Here any alternate approach is utterly lacking.

In the last analysis the only concrete reason given for rejecting Dr. Limmer's testimony is that his conclusion as to reasonable return would not permit Transit to maintain dividends at their present level. But his testimony in effect showed that it was not necessary to maintain such dividends to attract capital appropriate to the rate base.

And what testimony is there that the Company's present dividends are reasonable? Not a word. The Commission has

not even made a finding on the subject. On the face of it, a dividend equal to 100% of the present capital stock investment is at least dubious, if the public's interest is taken into account. Certainly the maintenance of such dividend is not a standard that permits the rejection of testimony built on facts,--built on a comparison, not with gas and electric utilities, but with other companies in the transit business of comparable size.

Clearly, the Commission erred in this proceeding and in this record in concluding that a return of \$660,146, which the staff estimated would result without a fare increase, was unreasonable and that a return of \$1,143,249 is fair and reasonable; and its decision must be reversed and remanded.

#### IV

#### THE COMMISSION ERRED IN FAILING TO ADHERE TO THE RETURN ON RATE BASE AND ATTRACTION OF CAPITAL STANDARDS PRESCRIBED BY STATUTE

The Commission erred in failing to adhere strictly to the capital attraction standard prescribed by the Franchise. The only standard offered by the Commission as the basis for a greater return is its own unsupported judgment, and that is not permissible.

That the Commission relied solely on its unsupported judgment is clear enough. The Commission's opinion first discusses a standard of earnings related to gross operating revenues and develops this as depending solely on Commission judgment (JA 11, 24). The Commission's opinion then turns to the

test of return on rate base; and concludes, disregarding all objective standards for determining the maximum allowable rate of return, that a 30% return on equity capital is reasonable "when consideration is given to the relatively low percentage of equity capital invested in the business and to the element of risk inherent in any investment in the transit industry" (JA 25). The Commission concludes (JA 27):

What constitutes a reasonable return is a question of fact, the solution of which calls for the exercise of sound judgment and common sense.

When such words represent the totality of the rate-making process they signify the failure of governmental process. Such a pretense of regulation, without considered standards, is a nullity and cannot support the fare increase order.

Section 4 of the Franchise states that Transit "should be afforded the opportunity of earning such return as to make the Corporation an attractive investment to private investors."

Similarly, Congress provided in a recent joint resolution approving an interstate compact between the District, Virginia, and Maryland for the regulation of transportation (hereinafter the "Compact")<sup>10/</sup> that the several utilities subject to the jurisdiction of the newly-established Washington Metropolitan Transit Commission (hereinafter "WMTC") "should be afforded the opportunity of earning such return as to make the carriers attractive investments to private investors."

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<sup>10/</sup> Act of Sept. 15, 1960, 74 Stat. 1031, 1040-41. Title II, Sec. 6(a)(4).

These sections prescribe that Transit should earn that return needed to attract capital on favorable terms (its cost of capital). This and only this return may Transit be allowed the opportunity to earn beyond its operating expenses under these statutes.

The attraction of capital standard of the statutes is not unique,<sup>11/</sup> but on the contrary is broadly recognized as the proper standard for fair rate of return that utilities generally should be allowed to earn, and indeed has been so recognized by this Court. Capital Transit Co. v. Public Utilities Commission, supra, and Washington Gas Light Co. v. Baker, supra. This standard is discussed further in Section V 1, infra.

V

THE RATE BASE MAY NOT EXCEED THE CAPITAL INVESTMENT  
OF TRANSIT IN ASSETS DEVOTED TO THE PUBLIC SERVICE

The Commission increased rates of fares to enable Transit to earn a return on a rate base of \$16,016,819 (JA 2-3, 25). Appellants submit that the rate base may not exceed \$9.2 millions,<sup>12/</sup> which is Transit's capital investment in 1956

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11/ For a recent exposition of the analytical and economic method commonly employed to obtain a regulated utility's cost of capital, see Howell, "The Rate of Return in Air Transport," 24 Law And Contemporary Problems 677 (1959).

12/ This is a maximum rate base. As shown in section VI 2, the rate base may properly be reduced by another \$2.8 millions. Under contract dated July 7, 1956, Transit purchased the operating authority and all assets of Capital Transit Co. On July 24, 1956, Congress granted Transit a new Franchise to operate in the District. The capital investment in road and equipment made by Transit amounted to \$7 millions (JA 87). New equipment has been added to this figure by Transit at an original cost of \$6.8 millions; there have been certain retirements; depreciation has been allowed on the investment at the rate of \$1 million per year; and today, the capital investment stands at \$9.2 millions (see Appendix B).

when it purchased the transit facilities previously operated by another company (plus Transit's additions less depreciation and retirements to date).

1. Transit's Return Is Determined By  
Transit's Investment, Not Another  
Company's Investment.

It is a basic rule of rate regulation that a utility is entitled to earn a return on its capital investment, its prudent investment in properties devoted to the public service. Transit and its investors have not invested capital to the extent of the book value of the assets in the hands of the former owner, Capital Transit Company; they are not entitled to a return on that book value. A prudent investment rate base is "the sum of those expenditures made by a public utility to enable it to serve the public which it has not yet had the opportunity to recoup from the public."<sup>13/</sup>

A utility is entitled to a return measured by "the cost to the utility of the capital required to construct, equip and operate its plant." See Brandeis, J. in State of Missouri ex rel. S. W. Bell Tel. Co. v. Pub. Service Commission,

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<sup>13/</sup>Kripke, "A Case Study in the Relationship of Law and Accounting: Uniform Accounts 100.5 and 107," 57 HARV. L. REV. 433 (1944). In some cases, Federal courts and commissions have disregarded subsequent purchase price by a new group of investors, but in those cases their investment included an amount exceeding book value as shown on the books of the former owner, and included intangible values, imprudent investment, or arbitrary write-up of assets, none of which appear in the present case. The subsequent investors are entitled to consideration of their investment to the extent that it is "prudent" investment. See e.g., Niagara Falls Power Co. v. Federal Power Commission, 137 F.2d 787, 794-95 (2d Cir., 1943), cert. denied 320 U.S. 792, reh. denied 320 U.S. 815.



262 U.S. 276, 291, 306 (1922). And see Federal Power Commission v. Hope Natural Gas Co., 320 U. S. 591, 603 (1944):

"The rate-making process under the Act, i.e., the fixing of 'just and reasonable rates', involves a balancing of the investor and the consumer interests. \* \* \* From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock (citation omitted) . . . . By that standard the return to the equity owners should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital."

The critical "end result" establishes the lawfulness of the rate from the investor or company standpoint. "It is a standard of finance resting on stubborn facts." Colorado Interstate Gas Co. v. Federal Power Commission, 324 U.S. 581, 605 (1945). The return on capital investment is the maximum allowable return that will apply, as in the present case, to "a company which had advantage of an economic position which promised to yield . . . an excessive return on its investment and on its securities." Market Street Railways Co. v. Railroad Commission of California, 324 U. S. 548, 566 (1945).

The Commission arbitrarily departed from its standard laid down in rate cases concerning the prior transit company that allowable earnings must be based on the capital actually invested in the enterprise. See Order No. 3422 of October 1,



1948: <sup>14/</sup>

For several years this Commission has employed the cost of capital method in arriving at a fair rate of return. Briefly, this method requires a determination of the actual cost of the debt capital and preferred stock capital, if any, and a reasonable return on the equity capital invested in the enterprise. This latter factor is premised in substantial part upon the investor appraisal of equity capital as measured by the market price of such capital in relation to earnings and dividends thereon. The employment of this principle in determining the fair rate of return, which the Commission believes is equitable to both investors in and patrons of the utility necessitates the application of the rate of return so determined to the capital actually invested.

The present case differs in a critical feature from Spiegel v. Public Utilities Commission, 96 U.S. App. D. C. 307, 226 F. 2d 29 (1955), cert. denied 320 U.S. 904 (1955), and 101 U.S. App. D.C. 93, 247 F. 2d 84 (1957). In the Spiegel cases the transportation assets continued to be owned by the same company, and the investment made by that corporate owner in these amounts remained the same. All that had changed was the identity of the persons owning stock in the transit company. The Commission continued to allow the company's original cost as the rate base, for historical cost and prudent investment were still one and the same, and it was eventually upheld in this Court. But that case provides no justification for allowing as rate base an amount in excess of the sums invested by the transit company.

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<sup>14/</sup> In the Matter of Application of Capital Transit Company for Authority to Change Certain of Its Rates of Fare, P.U.C. No. 3186/102, Formal Case No. 380, at page 14 of the printed order. Cited, but not fully reported PUR Annual, 1949, Section 265.

A fair and reasonable end result in the present case requires limiting Transit's earnings to a reasonable rate of return on that corporation's capital investment in used and useful property.

2. Transit's Depreciation Was Ultimately Based On Transit's Purchase Price And It Was Error To Use A Higher Basis For Computing The Permitted Return.

The \$7 million price paid by Transit reflected a substantial discount of over \$10 millions from the net book values of the properties (JA 12, 79, 83, 87). Net book value was about \$18 millions in 1956 (JA 87), and also at September 30, 1959 (JA 49).

Since August 15, 1956, the Commission has allowed Transit to record the purchased assets at the cost to Capital Transit, the previous owner, and to accrue depreciation upon the basis of that cost, at the same rate as that allowed to Capital Transit, for an annual allowance of over \$2 millions (JA 12-13). However, Transit was also required to write-off with periodic debits at an annual rate of \$1,033,904 the "acquisition adjustment" account--i.e. the \$10 millions excess of net original cost of properties recorded by Capital Transit over the cost thereof to Transit (ibid.). This write-off ordered by the Commission resulted in accrual of depreciation only to the extent of Transit's purchase price. The net effect of initially computing depreciation at \$2 millions and of requiring Transit to write-off the acquisition adjustment

account (at \$1 million per year) is to allow annual depreciation of \$1 million.

As the Commission stated in the present case, "depreciation is accrued on the basis of original cost [to predecessor] with an offsetting credit for amortization of the acquisition adjustment to effectively reduce the provision for depreciation to the basis of depreciation on the purchase price of the property [paid by Transit]." [Inserts in brackets supplied] (JA 13).

This net depreciation allowance is based on sound rate-making principles. Lindheimer v. Illinois Telephone Co., 292 U.S. 151, 167 (1934):

In determining reasonable rates for supplying public service, it is proper to include in the operating expenses, that is, in the cost of providing the service, an allowance for consumption of capital in order to maintain the integrity of the investment in the service rendered. [Emphasis added.]

See also Milwaukee & S. Transport Corp. v. Wisconsin Public Service Commission, 268 Wis. 573, 68 N.W. 2d 552 (1955).

Yet, the Commission arbitrarily departed from this sound principle when it computed rate base, not on the basis of Transit's investment, but on a higher figure which reflected a substantial part of the "original cost" to Capital Transit, as set forth in Section V 3.

3. The Commission Erred In Increasing The Rate Base To Take Into Account Any Contingent Liability For Conversion From Streetcar To An All-Bus Operation. The Rate Base Should Have Been Increased For This Item Only As To Amounts Actually Invested By The Company For This Purpose, And Not As To Amounts Obtained From Previous Ratepayers For This Purpose Or For Amounts That May Be Invested At Some Future Date.

In establishing Transit's rate base the Commission made several improper determinations, each of which operated to overstate proper rate base.

- (a) Error in increasing the rate base above "purchase price" paid by Transit by averaging with the "original cost" to Capital Transit.

In establishing a rate base as of the time that Transit purchased the assets, the Commission was presented with two views--Transit's view that the rate base was established at least by the cost to Capital Transit (referred to as the "original cost of the property") and the Staff's view that the rate base was established by the cost to Transit (referred to as the "purchase price rate base") (JA 81-82).

The Commission properly rejected Transit's proposal on the ground that it ignores the fact that the property was acquired by the present owners at substantially less than the amount at which it was carried on the books of the Capital Transit Company.<sup>15/</sup>

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<sup>15/</sup> JA 85. See also the findings accompanying Order 4480 Re D. C. Transit System Inc., 25 PUR 3d 371 (1958), incorporated by reference in part in the Opinion at JA 6-7.

Then the Commission rejected the staff view on the ground that it "gives no consideration to the effect, if any, on the purchase price of the assumed liability for track removal and repaving."<sup>16/</sup> In this proceeding the Commission used as its rate base an "average" of the "original cost" (to Capital Transit and the "purchase price" (paid by Transit for the properties) (JA 20, 23, 53).<sup>17/</sup>

The Commission's rejection of the staff approach reflects an important misconception. The proposal to use "purchase price" rate base does not ignore the contingent liability for track

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<sup>16/</sup> Ibid, and JA 23. The Commission here also argues that purchase price cannot be controlling of the rate base, since the predecessor company faced loss of its franchise and liquidation when Transit arrived on the scene in 1956. Of course, it might also be argued that Transit should not obtain a windfall return on its investment; but it is difficult to see how this factor should be compelling in the Commission's opinion, in view of the Commission's allowing depreciation based on the purchase price. In effect the Commission argues that rate base value must include some amount for good will or going concern values, a decision which is contrary to the Niagara Falls opinion, supra.

In any event, the Commission errs on the facts premising this argument. Negotiation by Transit with the predecessor company commenced only after the House had passed a bill to continue the operation of the predecessor company; this bill was passed by the House on May 17, 1956. The sale to Transit was consummated on July 7, 1956, after several groups had offered to purchase the predecessor company. See Representative Harris' comments, 102 Cong. Rec. 8290, ~~July 19~~<sup>May 17</sup>, 1956, id. at 13580, July 19, 1956, and the present record at JA 238.

<sup>17/</sup> As shown in Section V 3(b), the Commission's computation of the purchase price rate base at \$12.9 millions improperly includes approximately \$4 million of that portion of the acquisition adjustment which already has been written off.



removal and repaving. On the contrary, as soon as the Company actually invests some money for this purpose it is entitled on the purchase price theory to include this investment in the rate base, just as if it were a deferred installment of purchase price. Transit could thenceforth recover this investment both by increased depreciation allowances and by an increase of permitted "return" corresponding to the increase in investment.

What the Commission did through the averaging technique was to include additional millions of dollars in the rate base over and above the Commission's inflated calculation of the purchase price on the basis of a contingent investment. This additional sum inserted by the averaging technique, amounted <sup>18/</sup> in the current proceeding to a minimum of \$3,000,000.

Thus the Commission erroneously gave Transit the benefit of the same treatment as would have been properly forthcoming if Transit had actually been required by Congress or the Commission to make a cash deposit of an additional \$3,000,000 and to hold this fund in an earmarked account subject to the Commission's control to assure coverage of track removal and repaving expenses. But here neither Transit nor its investors have made any such investment for removal purposes, and they are receiving the benefit of such profitable investments as they receive on their non-transit funds generally.

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<sup>18/</sup> The "original cost" was computed by the Commission at \$19 millions, the "purchase price" at \$12.9, for an average of \$16 millions (JA 20).



There is no basis for giving Transit a return on a Transit investment before it is called upon to make that investment.

- (b) Error in eliminating (through an "amortization" approach) all recognition of the fact that Transit's purchase price was less than original cost to Capital Transit.

The Commission provided that the balance sheet which reflected property on the asset side at original cost (to Capital Transit), should also carry a liability, amounting in 1956 to \$10,339,041, captioned: "Excess of net original cost of properties recorded by predecessor owner over cost to present owner". See JA 12, 49.

This initial recognition, that the original cost was \$10,000,000 more than Transit's investment, was coupled with an order providing that this "liability" should be eliminated over a period of 10 years, through a reduction of expenses, of approximately \$1,000,000 per annum, captioned "Amortization of Acquisition Adjustment" (JA 12-13).

But this annual item did not in fact decrease the expenses of Transit below those properly recognized. It was merely used as an offset to depreciation reserve, and served to reduce depreciation expense from an artificially inflated figure (based on original cost to Capital Transit) to a proper figure (based on Transit's investment). (See Section V 2.)

The effect of this amortization has been to decrease year by year the amount shown on the balance sheet as the excess of

original cost over purchase price. The rate base thus has been permitted to move closer year by year to original cost (to Capital Transit) and increasingly higher than the purchase price (actually invested by Transit). The Commission's own calculation of the purchase price rate base is improperly inflated by approximately \$4 million representing that portion of the acquisition adjustment already amortized (JA 20-21).<sup>18A/</sup>

The amortized acquisition adjustment does not represent any additional investment by Transit, and was improperly used as a means of increasing the rate base. The reasons for such acquisition adjustment accounts were set forth by the Supreme Court as early as 1936, when the Federal Communications Commission prescribed its uniform system of accounts. A.T.&T. Co. v. United States, 299 U.S. 232 (1936). The FCC had required all utilities subject to its jurisdiction to show original cost (actual money cost) of properties when first devoted to public use, and in a separate account ("Telephone Plant Acquisition Adjustment") the difference between original cost and "the investment in such property by the accounting company itself" (299 U.S. at 238). The FCC required the latter account to be amortized as the Commission should subsequently direct.

The Supreme Court explained that the acquisition adjustment account had been adopted since transactions had occurred between affiliates at less than arm's length, or the "nuisance value" of a competitor had dictated the price paid for its assets. The utilities argued that the FCC was requiring a

<sup>18A/</sup> The Commission calculates the purchase price rate base by simply subtracting the unamortized portion of the acquisition adjustment from the net original cost of Transit's properties.

complete write-off of all acquisition adjustments. The Court read the F.C.C. directive differently and stated (299 U.S. at 240-42):

If subdivision (C) [requiring the write-off] had the meaning thus imputed to it, there would be force in the contention that the effect of the order is to distort in an arbitrary fashion the value of the assets. But the imputed meaning is not the true one . . . . On the contrary, only such amount will be written off as appears, upon an application for appropriate directions, to be a fictitious or paper increment.

Thus, assuming arm's length bargaining, the utility is entitled to a return on and recovery of its actual investment. The purchase price of the properties is not subject to any reduction based on a lower original cost (A.T.&T.--except in case of a "fictitious or paper" difference). And the utility may <sup>19/</sup> not obtain any increase based on a higher original cost.

(c) Error in referring to track removal reserve as a basis for increasing rate base.

As already noted the Commission did not embarrass Transit by reducing its proper annual expenses by the amount of acquisition amortization but used this amount (approximately ~~\$1.~~ \$1. million per annum) to reduce an inflated depreciation expense to a proper figure. (See Section V 2)

In addition the Commission permitted Transit an annual expense of over \$1,000,000 to be set aside in a book "Reserve

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<sup>19/</sup> Recently the Interstate Commerce Commission adopted this view of the A.T.&T. case, and prescribed by regulation that for accounting purposes properties which are purchased in a complete transfer of the operation from one carrier to another (as in the present case) must be recorded at the purchase price, or fair market value if less than the price. 25 F.R. 1251, effective April 1, 1961.

for Track Removal and Repairing.") (JA 12-13, 49).

As already seen, this reserve now stands far in excess of amounts already expended by Transit or forecast for expenditure in any reasonably foreseeable future.

Instead of being abashed by this over-reserve the Commission's opinion deftly twists it into an additional justification for enlarging the rate base, and implies that Transit is entitled to a return on the amounts held in this reserve (JA 12-13, 51).

But the amounts in the track removal reserve do not represent an investment by Transit. They are not even a transfer from earned surplus. This reserve is merely an accrual of amounts contributed by the farepayers, and this reserve has no pertinency as a justification, express or implied, for enlarging Transit's rate base. See Sec. VI 2, infra.

(d) Error in using \$10,000,000 "assumed" liability as basis for increasing rate base.

The persisting fallacy in the Commission's reasoning is this: even though the amounts in the acquisition adjustment account and track removal reserve may represent an assumed obligation of Transit, i.e. an obligation to pay more for the assets than the cash paid to Capital Transit, until Transit devotes some part of capital raised from investors to this contingent liability, it stands as a cost-free obligation. There are no capital costs of any kind attaching to this obligation at the present time. Transit has sold neither bonds

nor stock to cover this obligation; it neither pays interest nor requires earnings to pay dividends on account of this obligation. There is no showing on this record that capital must be attracted in the future period, or in any particular period, on account of this obligation. The farepayers should not be required to pay either a return or depreciation on such contingent obligation.

The acquisition adjustment account does not represent any capital investment by Transit at the present time, but merely an "excess" in the predecessor's book cost over the cost to Transit. The track removal liability is contingent; until the costs are actually incurred, Transit merely has the benefit of an initial donation of assets (in that the cash paid to Capital Transit was less than that company's original cost). As to Transit's building of a track removal reserve, that merely represents a contribution of capital made by farepayers in the form of an annual operating allowance. Accordingly, these amounts represent either a donation of capital by Capital Transit, or a contribution by Transit's farepayers through operating expenses. In either event the amounts are now cost-free capital of Transit and are not properly includable in the rate base.

## VI

THE COMMISSION'S VALUATION OF THE RATE BASE AT OVER \$16 MILLIONS IS ARBITRARY, CAPRICIOUS, AND UNREASONABLE

Assuming arguendo the Commission may establish the rate base at a higher figure than Transit's investment, this Court



should, nevertheless, hold that the determination of a rate base in excess of \$16 millions on the present record is excessive and unlawful.

1. A Valuation Of The Rate Base At Over \$16 Millions Is Unsupported By, And Is Contrary To, The Substantial Evidence Of Record Which Indicates A Valuation At Around \$12.5 Millions Is Fair and Reasonable.

The substantial evidence of record is that a rate base valuation of around \$12.5 millions is fair and reasonable; the Commission unreasonably and arbitrarily valued the rate base at over \$16 millions.

Witness Falk of the Commission's staff developed for the record a rate base averaging Transit's purchase price (increased by the amount of the amortized acquisition adjustment account) and original cost to Capital Transit (JA 53).

The Commission erred as a matter of fact in considering this average as witness Falk's "proposed" or "recommended" rate base (JA 19, 22). On the contrary, the record clearly shows that although this witness computed the average for the information of the record, his expert opinion was that only the purchase price provided the basis for a proper valuation.

See JA 141:

Q. [By Mr. Bebachick] In your personal opinion, Mr. Falk, is not a purchase price valuation of the rate base the proper method to employ in this proceeding?

A. [By Mr. Falk] I so testified in a previous case, but the Commission has ruled three times that this is the proper procedure and I respect the decision of the Commission and have proposed this method in this case.



Q. I see. But, aside from following their precedent, since you are qualified as an expert on this matter, I am trying to elicit whether your personal opinion remains the same as it was in the previous proceeding.

A. My personal opinion still remains the same; yes.

Q. Therefore, as far as your personal opinion goes, the proper rate base in this proceeding would be the figure \$12,892,112, in the second column on Schedule 4 here.

A. That would be the rate based on purchase price; yes. 20/

The only other computation of a rate base in this proceeding was made by witness Harris, a transportation accountant, who similarly testified that a rate base valuation of \$12.6 millions was fair and reasonable. This witness testified to the following effect: the acquisition adjustment represented in part a valuation reserve, on the order of a depreciation reserve, to offset the losses to be incurred at the retirement of the streetcar properties, and in part a donation of assets to cover the assumed liability for track removal (after tax credits). The \$10 millions of book reserves, including the acquisition adjustment account and the reserve for track

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20/ The witness' computation is clearly overstated by more than \$600,000 since he admittedly failed to adjust his depreciation estimate according to the Commission's Order 4577 of September 30, 1959, reported 30 PUR 3d 405, on the grounds "the matter is still in litigation and until it is decided I didn't make the adjustment" (JA 143-144). He did not consider the adjustment improper (*ibid*). In any event, the validity of Order 4577 has subsequently been upheld on review by this Court. D. C. Transit System, Inc. v. Public Utilities Commission, No. 15967, per curiam decision of May 18, 1961.

removal and repaving, at the beginning of the annual period were sufficient, (1) to provide for the retirement of all remaining rail properties without any further depreciation of such properties, and (2) to provide for the full future cost of all track removal and repaving of \$10 millions, as estimated by the Commission, after considering the effect of such expenses as a tax deduction (JA 70-71, 209-210).

The foregoing is the substance of the entire testimony on rate base. Transit witnesses presented no evidence to develop a net investment rate base (JA 20), and merely gave a conclusory opinion regarding such a base.

There is no substantial evidence in support of the Commission's determination of a rate base giving equal weight to the purchase price and to the original cost of the properties to the company first devoting the properties to the public service.

2. The Commission's Rate Base Of Over \$16 Millions Unlawfully Includes Amounts Which Have Already Been Paid By The Farepayers As Operating Expenses

To reach \$16 millions of property values determined by the Commission as a rate base it is necessary to add to the debt and equity accounts the substantial sums that have been accrued as reserves through annual charges to revenues.

This Court has clearly held that an item once treated as an operating expense is not includible in the rate base.

Pennsylvania Water & Power Co. v. Federal Power Commission, 89 U.S. App. D. C. 235, 193 F.2d 230, 243 (1951), aff'd

343 U.S. 414 (1952). See also City of Philadelphia v. Pennsylvania P.U.C., 173 Pa. Super. 38, 95 A. 2d 244, 251 (1953). The Commission erred in determining a rate base so high as in effect to include operating reserves built up through operating expenses.

For detail underlying the foregoing point, reference should be made to Transit's balance sheet (JA 49) which shows the following accounts on the right-hand side:

Debt obligations--due in one year	\$ 934,648
Other "current liabilities"	3,121,418
Debt obligation--due after one year	2,765,158
Reserve for Injuries and Damages	1,868,760
Reserve for Moving and Relocating	325,000
Reserve for Track Removal and Repaving	3,216,286
Acquisition adjustment account	7,108,091
Capital Stock and Surplus	3,153,101

The debt and equity (even including debt due in one year) total under \$6.4 millions. The end result of valuing the rate base properties at over \$16 millions is the inclusion in the rate base of such operating reserves as the "Reserve for Track Removal and Repaving" or the "Reserve for Injuries and Damages", both of which were built up by annual charges. These reserves must be deducted from the rate base figures to avoid double-charging the farepayers to the extent of the return element allowed on the reserves, and the Commission and the Court below erred failing to require such a deduction.

Earlier we referred to \$9.2 millions as the maximum allowable rate base in this proceeding; the figure of \$9.2 millions represents Transit's present investment in its

property. However, the capital investment of Transit's investors presently amounts to less than \$6.4 millions, the sum of the debt (even including obligations due in one year), capital stock, and earned surplus (JA 69).

The remaining \$2.8 millions in Transit properties derives from Transit's use of cash funds that were built up due to the amounts improperly allowed to Transit as non-cash expense allowances, such as the annual provision for track removal and repaving. Transit took the excess cash arising out of these allowances and paid off substantial debt obligations (JA 115-116); thus, rather than being fully offset by cash funds held in an earmarked account (see JA 13), the present operating reserves are partially offset by used and useful property on the lefthand side of the balance sheet.

Therefore, although \$9.2 millions of prudent investment represents a maximum limit to the proper rate base, \$9.2 millions in fact overstates a proper rate base, since the company is not entitled to a return on properties already fully paid for by the farepayers. The figure of \$9.2 millions represents capital contributions of both the investors in Transit and of the farepayers. A proper rate base would be under \$6.4 millions, the total capital investment of Transit's investors. To the extent that the investors increase their investment in Transit, the rate base would be correspondingly increased.

In the meantime removal of these operating reserves from the rate base results in a sound rate base, composed of capital contributed by investors, and the allowance of a just and proper return on the capital investment, i.e. that part of the prudent investment in assets contributed by the capital investors.

3. The Rate Base Unlawfully Includes Abandoned Properties For Which Transit Has Already Received Full Compensation.

The rate base includes an item of \$5,121,644 as the net undepreciated cost of rail properties at December 31, 1959. This entire amount was retained in the rate base calculated for the 12 months ending December 31, 1960, even though \$2,530,092 (or 49.4% thereof) was admittedly abandoned on January 3, 1960. This \$2,530,092 figure was included in both rate base calculations by the Commission witness Falk--the one based on original cost and the one based on purchase price and, therefore, obviously was included in the "average" rate base utilized by the Commission. See JA 52-54, 142-143.<sup>21/</sup>

This Court has clearly held that the Commission may not lawfully include abandoned property in the rate base of a regulated

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<sup>21/</sup> These figures explicitly appear in Exh. 39, Schedule 3, (JA 52) (depreciation expense) and are also reflected in the rate base figures in Schedule 4 (JA 54) as was admitted by Commission's expert Falk (JA 142-143).



utility unless the investors have not been compensated for the risk of obsolescence of these properties. Washington Gas Light Co. v. Baker, supra. The evidence of record makes it abundantly clear that Transit's investors have been fully compensated in several ways for the early abandonment of the rail properties.

Transit's investors are not entitled to a further return on the abandoned rail properties. Transit purchased the assets and accepted a Congressional franchise which specifically required a conversion to an all-bus operation within seven years, unless the period were changed by order of the Commission. As described in Section II.1., supra, it was precisely because this fact was known that Transit (and its investors) received the benefit of a discount of more than \$10 million from the book cost of the transit properties purchased. This discount of \$10,000,000 fully compensated Transit for the future obsolescence of rail equipment. This was Transit's arm's length calculation of the burden of withdrawing rail equipment, which cannot now be rejected by Transit. Moreover, as to the adequacy of the \$10,000,000 figure over the Commission's projected conversion cost, see testimony of Harris, discussed at Sec.VI.1., supra. The feature of obsolescence can in no way justify a return to Transit higher than its actual investment in transit properties--including any sums actually expended for conversion.

Even if the discount obtained in 1956 were not fully adequate at that time to compensate for the early retirement of rail properties, there has been full compensation for all risks in the returns since 1956, returns substantially above the cost of



attracting capital. The entire capital stock in Transit, issued in 1956, represents an investment of only \$500,000. Dividends paid since formation to the date of the hearing aggregate \$1,140,000--an average yield of 66% per annum (JA 24, 65, 117-9). Total earnings since formation (after dividends and taxes) exceeded \$3,000,000 in 38 months time, reflecting average earnings in excess of <sup>95</sup>~~25~~% per annum as a percentage of total equity (investment by stockholders plus retained surplus) (JA 66).

The Commission plainly erred in including abandoned rail properties not used and useful in the public service in the rate base just as it erred in continuing to permit regular depreciation on and special amortization for abandoned properties.

## VII

### THE RATE ORDER DERIVES NO SUPPORT FROM THE COMMISSION'S REFERENCE TO A GROSS OPERATING REVENUES METHOD

The Commission referred to a rate of return on the gross operating revenues of Transit in this proceeding. Its findings and conclusions are unclear. In any event in view of the Franchise, the Commission's Order and Opinion cannot be supported by a reference to a gross operating revenues method.

1. The first conclusion listed in the Order herein was (at JA 2) "That the gross operating revenue method should be utilized to fix rates in this proceeding."

This apparently straight-forward pronouncement was undercut by the rest of the Order and Opinion.

In fact, the Commission, (a) rejected Transit's contention that gross operating revenue method was a sufficient basis for fixing rates, which obviated rate base testimony (JA 10-11); (b) expressly stated in its third conclusion that the "rate base rate of return" method of fixing rates "affords a sound basis for testing the reasonableness" of rates (JA 2); and (c) actually used the system rate base method as the ultimate test of the reasonableness of the return element, and purported to use the gross operating revenue method as a rough means of verifying the result, not sufficient to constitute an independent ground of decision (JA 11, 24). Shorn of excess verbiage, it is clear that both the Order and the Opinion contain but one objective test--and that is the resulting return on system rate base.

The Commission's artful use of operating ratio as a means of blunting criticism or of deriving an aura of reasonableness (from a consumer point of view) was not intended by the Commission as a determination to substitute earnings as a percentage of revenues, or any "operating ratio" (the reciprocal of such percentage) as the pertinent method of regulation of Transit and to install it as the governing and dominant method.

2. Indeed, the Commission could not properly have adopted any revenue method without findings supporting a determination that "conditions warrant" the shift in Commission approach. Congress prescribed as an ultimate standard the setting of rates sufficient to cover expenses and attract capital. Congress

permitted a shift from percentage of rate base to percentage of revenues as an instrument of achieving that ultimate standard, but provided for such shift only if or as "conditions warrant".

Section 4 contemplates that the Commission will continue to use the orthodox rate-of-return-on-rate-base method of rate-making and to gauge the fairness and reasonableness of Transit's income as a percentage of its net investment. Thus, the section speaks of "shifting" to a new and untried method only "as conditions warrant" or "if conditions warrant".<sup>24/</sup> "Conditions warrant" means when economic conditions call for gross operating revenue base in order to enable Transit to have the opportunity of earning such return as it needs to be an attractive investment to private investors.

There is no evidence of record that Transit is inhibited from raising capital on favorable terms, or from earning a fair return if the Commission uses system rate base, or of any economic condition warranting the use of the revenue method. And to the extent the Commission purported to find that conditions

Note: Footnotes 22 and 23 omitted.

<sup>24/</sup> It should be noted that the Franchise, but not the Compact, provides for a "shift" to the revenue method. Even then, the applicable standard is still that of the rate needed to attract capital stated in the first sentence of Section 4. The revenue method is referred to in the Franchise as an inducement to a new operator in the event that a reasonable return on investment cannot make it an attractive investment to private investors. The Compact, which is intended to consolidate the regulation of all companies in the metropolitan area, makes no reference whatever to such an inducement. See Section IV, supra.

warranted a shift, it erred as a matter of law.<sup>25/</sup>

The conclusion that use of a system rate base under section 4 is required until a departure to operating ratio method has been justified by the Commission is underscored by section 9. The latter section defines "a 6-1/2 percentum rate of return" for the purposes of determining Transit's liability for motor vehicle fuel taxes in the District of Columbia, as "a 6-1/2 percentum rate of return . . . on the system rate base of the Corporation, except that with respect to any period for which the Commission utilizes the operating ratio method to fix

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<sup>25/</sup> The Commission in its Opinion (JA 7-10) unlawfully relied upon the extent of progress in Transit's conversion program as raising conditions warranting the use of the revenue method. This reading of the Franchise is not consistent with any reasonable reading of the language of the Franchise. Moreover, the basis of the Commission's opinion on this point are letters to Transit of January 27, 1959 (JA 43-45), which the District Court held not to be a final order (See JA 63-64 for a copy of this order), and which was sent after ex parte conferences with Transit (JA 126-128). These letters were admitted over objection (JA 129).

The Commission made no findings to support its conclusion that Transit's conversion program somehow raises conditions warranting the use of the revenue method, nor is there any record support for such findings even if made. Even if it be conceded arguendo that "conditions" of section 4 refer to Transit's progress in converting from a streetcar operation to a bus operation, the use of the gross operating revenue method is still not "warranted" within the meaning of the section nor even in a colloquial sense of the term. The Transit witness Flanagan himself testified that conversion will progress regardless of whether the revenue or operating ratio method is used by the Commission (JA 247-249). Further, it is the position of Transit and the testimony of its own witness that a return of 6-1/2% of revenues is not needed to attract capital on favorable terms (JA 244, 246-247), and the company steadfastly maintained it was not asking for 6-1/2% of revenues at this time (ibid.). Hence, a return of 6-1/2% of revenues is not warranted within the meaning of the Franchise.

the rates of the Corporation, such term shall mean a return of 6-1/2 percentum . . . based on gross operating revenues."

[Emphasis added]

In providing for a determination as to whether and when conditions would warrant use of the operating ratio method, Congress presumably legislated in light of the decisions of agencies utilizing that method, such as the Interstate Commerce Commission. The ICC uses the ratio typically in cases involving general rate increases for regional groups of motor carriers. For example, in New England Motor Rate Increases, 1955, 66 M.C.C. 215 (1956), increases affecting 800 motor carriers were filed. Financial data of 135 Class I and 226 Classes II and III were considered (id. at 219, 220). The ICC could merely conclude that "[t]he precise effect of the 6-1/2 percent increase [here sought] cannot be calculated, but it is clear that it would do little more than prevent respondents' average operating ratio from increasing." (id. at 220).<sup>26/</sup>

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<sup>26/</sup> Proceedings involving the data of 73 carriers, or 44, or even 188 are not uncommon. See New England, 1946 Increased Rates, 47 M.C.C. 509, 513 (1947); Central Territory General Increases, 49 M.C.C. 4, 12 (1948); and Increased Common Carrier Truck Rates in the East, 42 M.C.C. 633 (1943).

The Interstate Commerce Commission's statutory authority to rely upon operating ratio in setting fares of a transit company experiencing severe losses was upheld in The County Board of Arlington, Virginia v. United States, 101 F. Supp. 328 (E.D. Va., 1951); but, the Court there noted that plaintiffs had conceded that the ICC findings were supported by evidence, and expressly stated, "we are not deciding the merits of the rate case".



Only a handful of the State commissions refer to an operating ratio standard in their regulation of transit companies, and then typically only in relation to some rate of return on investment.<sup>27/</sup> As the present Commission found, "there is no formula or method of computing" the return on revenues; hence, it found that such a return must be the sole "result of Commission judgment" (JA 11, 24). For example, the company's witness could present no specific criteria for a return on revenues (JA 125-126).

But the Commission could not lawfully depart from the rate base method without a showing that its shift in method did not produce an unreasonable result from the standpoint of the consumer. City of Detroit, Michigan v. Federal Power Commission, 97 U.S. App. D.C. 230 F. 2d 810 (1955), cert. denied 352 U.S. 829 (1956). No such finding or conclusion of the Commission appears in this proceeding, nor could lawfully be made in view of the terms of Transit's franchise (discussed above) and the substantial evidence of record.

The substantial evidence of record in this proceeding negates any present showing of conditions warranting the use of the gross operating revenue method. Staff witness Roberts testified that he would not recommend the use of such a method

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<sup>27/</sup> E.g. Re Long Beach Motor Bus Co., 12 PUR 3d 198, 204 (Cal. P.U.C., 1955); Re Honolulu Rapid Transit Co., 90 PUR NS 129 (Hawaii P.U.C., 1951); Re Duke Power Co., 12 PUR 3d 300 (N.C.U. Com'n., 1956); and Re Milwaukee Electric Railway & Transport Co., 91 PUR NS 82 (Wis. P.S.C., 1951).



at this time (JA 130-131), and that in any event the "cost of capital"--i.e. the return on investment demanded by investors--is the ultimate test of fair earnings (JA 135-139). Witness Limmer, a transportation economist, presented a detailed analysis of Transit's cost of capital and testified that the "operating ratio" method (or its reciprocal, the revenue method) provides no valid measure of Transit's needed earnings (JA 162). In the witness' expert opinion, no economic conditions now warrant the use of the revenue method or any operating ratio standard (JA 169-170, 209), and this ratio does not indicate profitability (JA 61-62, 160-162). Thus, Exhibit 46 (JA 61-62) shows that several industries with very low returns on revenue (1%-2%) are, nevertheless, highly profitable, with returns of 15% on net assets.

The only contrary voice was witness Curtin, who testified for Transit after only one week's preparation (JA 253-254), made no studies of Transit for purpose of this proceeding (JA 252-253), and merely presented an overall conclusory judgment that the particular ratio of expenses to revenues of 93.5% is reasonable for any transit company. His opinion was based largely on the ratios adverted to in a selected list of State commission decisions without reference to the return on rate base these commissions might have used as their governing standard. The Commission properly disapproved witness Curtin's conclusion (JA 26-27).

Similarly, there is no substance in the testimony of Transit's Vice President Flanagan. This was mere conclusory testimony that the company was now entitled to a revenue base since it had complied with the ex parte letter of January 27, 1959 (JA 44-45), sent from the Commission on this matter. That ex parte letter was not a final order, and it cannot serve as a basis for a finding in an adversary proceeding. See note 25, supra.

On the other hand, the irrelevance of the conversion program to the question whether "conditions warrant" shifting the rate-making method to a percentage of revenues is underscored by Flanagan's testimony that the conversion program will progress regardless of whether rate base or operating ratio is used by the Commission (JA 249).

Clearly Congress did not authorize the Commission to make this shift whether or not "conditions warranted" in its judgment. Equally clearly, Congress did not authorize the Commission to make an arbitrary decision that "conditions warranted". Equally clearly, the Congress did not permit the Commission to make a bare determination that "conditions warranted" as a matter of its own ipse dixit without any opportunity for the Courts and Congress to consider the basis upon which the Commission has made their determination and without any opportunity for consumers to present reasoned arguments and evidence on the underlying issues as to whether "conditions warrant".

## VIII

### THE COMMISSION COMMITTED OTHER ERRORS IN THIS PROCEEDING

The Commission is charged with fixing rates that are reasonable to consumers. It has a duty to give consideration to activities of Transit's management that imprudently and unwarrantedly increase costs or decrease income, to test the reasonableness of return in the light thereof, and to make appropriate orders relating thereto. The Commission erred in failing to discharge that duty, as appears from a consideration of two illuminating actions of Transit's management.

1. This was the first rate proceeding after the 1958 rate proceeding. In the meantime--in 1959--a reorganization was put into effect by Transit's management. The parent company of Transit, formerly known as TCA Investing Company, changed its name to D. C. Transit System, Inc., a Delaware corporation and split its 200 shares into 2,500,000 shares outstanding. The grandparent company (Transportation Corporation of America) thereupon engaged in selling the Delaware company stock, based upon Transit's earnings, at 40 to 50 times its cost, to obtain windfall capital gains. On a sale to the public of 350,000 shares at \$10 per share, there was a capital gain of over \$3,100,000--and this in three years' time! The evidence of record establishes that this reorganization plan would inhibit Transit from raising capital for its public utility needs within the District of Columbia. See JA 55-56, and the testimony of witness W. Roberts at JA 149-151.

The Commission has chosen to overlook the plain fact that Transit's management has launched the sale of stock on a basis that capitalizes the high earnings and dividends in the early years of Transit's operation when Transit was able to avoid the impact of careful supervision. These high initial stock prices will impair Transit's standing whenever the regulatory authority calls a halt to the excessive earnings. And Transit has not even received the benefit of the high prices, since they inured to the advantage not to Transit but of Transit's grandparent and interlocking management. The situation is further inflamed by the fact that whatever earnings are permitted to Transit will be sponged up by the huge number of shares in Transit's parent brought about by the reorganization plan. The Commission was under a duty to protect both Transit and the public, by calling a halt to the pressure generated by this plan for ever-increasing revenues and fares. The Commission's bare "judgment" approach enabled it to avoid coming to grips with this problem. This financial history was ignored by the Commission although it is of obvious materiality as negating any sound claim of need for enhanced revenues for the purpose of attracting capital.

2. The Commission erred in failing to give effect to the fact that Transit keeps cash deposits of \$1.5 million in New York City banks without drawing interest, and in excluding evidence as to whether officials and stockholders of Transit and its parent and grandparent companies are obtaining benefits

from such banks. See JA 130, 242-243.<sup>28/</sup>

Transit is charged with conducting all of its activities in an efficient and economical manner. The funds obtained by Transit from its patrons must be utilized for their benefit, and not to assist Transit's grandparent in its aviation operations. At the very least, the Commission erred in not debiting Transit's income with constructive interest in an amount equal to that which such funds might have been earned if invested in short-term government securities.

#### CONCLUSION AND PRAYER

FOR THE FOREGOING REASONS, appellants respectfully pray this Court to,

1. Reverse the Order of the District Court affirming the Commission's decision;

2. Remand to the District Court with instructions to issue an order

- (a) Vacating the Commission's order of March 2, 1960, and ordering the Commission and Transit to discontinue the fare instituted by Transit (effective

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<sup>28/</sup> Subsequent to the hearing it was learned by the plaintiffs that on October 23, 1958, Transportation Corporation of America issued \$1,100,000 of 5-1/2 percent convertible subordinated debentures due October 1, 1968, to the latter. Transportation Corporation of America, Annual Report, 1959, p. 16. The Trustee under the Indenture is Federation Bank and Trust Company, a bank in which Transit has made substantial non-interest bearing deposits (JA 130).

March 6, 1960) pursuant to the authorization and direction in the said Commission's order, and to restore the status quo ante by reverting to the fare in effect in the District of Columbia prior to March 2, 1960.

(b) Requiring the Commission to order the Company to fund and account for the revenues resulting from the fare increase since its effective date March 6, 1960, to be available as may be hereafter ordered for the benefit of the farepayers;

(c) Ordering Transit to pay counsel for appellants, including appellants for their activities as counsel pro se, a reasonable attorneys' fee taking into account benefit to farepayers, and costs of litigation, including reasonable fees for expert witnesses, before the Commission, the District Court and the Court of Appeals;

(d) Remanding for further proceedings not inconsistent with the decision of this Court 29/

3. And such other and further relief as the Court shall consider just and proper.

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29/ Upon remand to the Commission, the Washington Metropolitan Transit Commission may, in its discretion, take over the final disposition of this proceeding. See Compact, Title II Section 23.



In the event the Court affirms the District Court, taking into account the nature of appellants and the questions raised, that no costs be assessed against appellants.

Dated this 4th day of October, 1961.

Respectfully submitted.

Of Counsel

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## APPENDIX A

### STATUTE INVOLVED

The sections of Transit's Franchise, Act of July 24, 1956, ch. 669, 70 Stat. 598, involved in this appeal are as follows:

SEC. 4. It is hereby declared as a matter of legislative policy that in order to assure the Washington Metropolitan Area of an adequate transportation system operating as a private enterprise, the Corporation, in accordance with standards and rules prescribed by the Commission, should be afforded the opportunity of earning such return as to make the Corporation an attractive investment to private investors. As an incident thereto the Congress finds that the opportunity to earn a return of at least 6-1/2 per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on either the system rate base or on gross operating revenues would not be unreasonable, and that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible and as conditions warrant; and if conditions warrant not later than August 15, 1958. It is further declared as a matter of legislative policy that if the Corporation does provide the Washington Metropolitan Area with a good public transportation system, with reasonable rates, the Congress will maintain a continuing interest in the welfare of the Corporation and its investors.

SEC. 7. The Corporation shall be obligated to initiate and carry out a plan of gradual conversion of its street railway operations to bus operations within seven years from the date of the enactment of this Act upon terms and conditions prescribed by the Commission, with such regard as is reasonably possible when appropriate to the highway development plans of the District of Columbia and the economies implicit in coordinating the Corporation's track removal program with such plans; except that upon good and sufficient cause shown the Commission may in its discretion extend beyond seven years, the period for carrying out such conversion. All of the provisions of the full paragraph of the District

of Columbia Appropriation Act, 1942 (55 Stat. 499, 533), under the title "Highway Fund, Gasoline Tax and Motor Vehicle Fees", subtitle "Street Improvements", relating to the removal of abandoned tracks, regrading of track areas, and paving abandoned track areas, shall be applicable to the Corporation.

SEC. 9. (a) Except as hereinafter provided, the Corporation shall not, with respect to motor fuel purchased on or after September 1, 1956, pay any part of the motor vehicle fuel tax levied under the Act entitled "An Act to provide for a tax on motor vehicle fuels sold within the District of Columbia, and for other purposes", approved April 22, 1924, as amended (D.C. Code, title 47, chapter 19).

(b) For the purposes of this section--

(1) the term "a 6-1/2 per centum rate of return" means a 6-1/2 per centum rate of return net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on the system rate base of the Corporation, except that with respect to any period for which the Commission utilizes the operating ratio method to fix the rates of the Corporation, such term shall mean a return of 6-1/2 per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, based on gross operating revenues \* \* \* .

PRESENT PRUDENT INVESTMENT IN TRANSIT'S  
ROAD AND EQUIPMENT

		Reference
1.	Purchase price of properties in 1956 \$7,699,881	JA 87
	Retirements to date:	
2.	Retirements at prior owner's cost \$ 5,738,189	P. 2 hereof, col.5
3.	Avg. bk. cost of properties over period 48,195,107	P. 2 hereof, col.1
4.	Percentage of bk. cost retired 11.9% (Line 2 ÷ Line 3)	
5.	Estimated Retirements (Line 1 x Line 4) 916,386	
6.	Additions at Transit's original cost 6,786,780	P. 2 hereof, col.6
7.	Depreciation & Amortization to date 5,293,473	
8.	Investment in Materials & Supplies 774,508	JA 20, 53
9.	Construction Work in Progress 467,752	JA 20, 53
10.	Present Investment in Properties \$9,519,062 (Line 1 - Lines 5 & 7 ÷ Lines 6,8,9)	
11.	Less investment in non-mass transp. and allocation of acq. adj. 359,616	JA 20, 53
	PRESENT PRUDENT INVESTMENT IN ASSETS DEVOTED TO THE PUBLIC SERVICE \$9,160,446 **	

\*Depreciation of \$8,974,903 (page 2 hereof, column 3) less amortization of acq. adj. of \$3,681,430. The latter figure equals the total amortization of \$4,178,695 (page 2, column 4) reduced by the percentage shown in Line 4 of 11.9%, representing retired properties (or \$497,265).

\*\*This figure might be further refined, for just as the Commission's "purchase price" rate base overstates Transit's investment in used and useful property, so a rate base of \$9.2 millions, 1) includes abandoned properties, discussed at page 24, supra, and 2) fails to account for the sale of certain properties as ordered by the Commission (see page 54, supra).

# COMPUTATION OF ADDITIONS TO AND RETIREMENTS FROM TRANSLIT'S PROPERTIES SINCE 1956

	Data Obtained From Refs.				Constructed From		Reference
	Avg. Book Investment (1)	Avg. Depreciation Res. Bal. (2)	Bk. Depreciation in Period (3)	Amortization of Acq. Adj. (4)	Columns (1)-(4)**		
					Retirements (5)	Additions (6)	
Bal. at 8/31/56			\$ 91,869	\$ 43,079			Exh. 91
Aug. '56-Aug. '57	\$47,724,645	\$30,466,429	\$2,031,482	\$1,033,904	\$ 202,028	\$ 646,512	P. U. C. 3592, Order of 11/27/57 (Exh. 91)
Aug. '57-Aug. '58	48,222,351	32,073,270	2,059,859	1,033,904	453,018	950,724	Id., Order of 11/13/58 Schedules 2 & 3
Aug. '58-Aug. '59	47,014,652	30,537,255	2,100,678	1,033,904	3,636,693	2,428,994	Id., Order of 11/13/59 Schedules 2 & 3
Sept. '59-Dec. '60*	49,818,778	31,476,647	2,691,015	1,033,904	1,446,450	2,760,550	Id., JA 51, 53, 54
Totals	\$48,195,107	\$8,974,903	\$4,178,695	\$5,738,189	\$6,786,780		

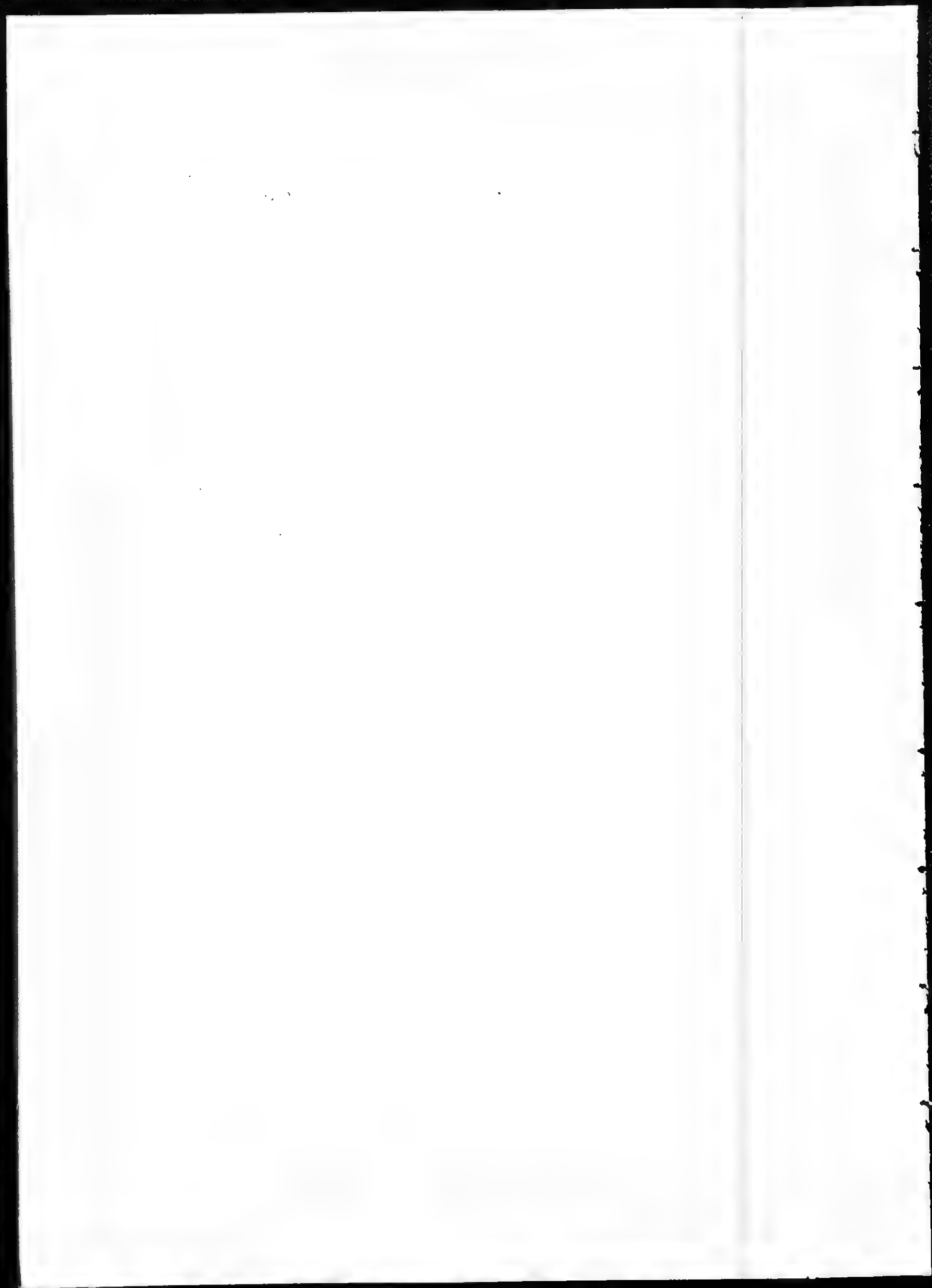
\*Present amount in column 3 plus prior balance in column 2 less present balance in column 2. This follows from basic formula that present depreciation reserve (present column 2 balance) equals prior depreciation reserve (prior column 2 balance) plus current depreciation (column 3) less retirements (column 5). However, for fiscal year 1956-1957, amount in column 5 was taken from order of 11/27/57, Exh. 91 herein.

\*\*Present column 1 balance plus present column 5 amount and less prior column 1 balance. This follows from the basic formula that present book value (present column 1 balance) equals prior book value (prior column 1 balance) plus additions (column 6) less retirements (column 5). However in fiscal 1956-1957, the amount in column 6 was taken from the order of 11/27/57, Exh. 91 herein.

\*As shown on JA 51-54; excludes any amount for the month of August, 1959.

\*\*As shown on JA 54.





237

BRIEF FOR APPELLEE PUBLIC UTILITIES COMMISSION

UNITED STATES COURT OF APPEALS  
For The District Of Columbia

No. 16,454

LEONARD N. BEBCHICK  
and  
LEONARD S. GOODMAN,

v

PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA  
and  
D. C. TRANSIT SYSTEM, INC.

United States Court of Appeals  
For the  
District of Columbia Circuit

FILED

NOV 28 1961

*Joseph W. Stewart*  
CLERK  
Appellants,

Appellees.

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Appeal From The United States District Court  
For The District Of Columbia

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CHESTER H. GRAY  
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GEORGE F. DONNELLA  
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ANDREW G. CONLYN  
Counsel

Attorneys for Appellee  
Public Utilities Commission  
District of Columbia  
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Washington 4, D. C.

### QUESTIONS PRESENTED

In the opinion of appellee Public Utilities Commission the questions are:

1. Will the Court entertain and rule upon an appeal from a rate order of the Commission, when such order has been superseded by a subsequent order based upon a later rate proceeding?

2. Absent error as a matter of law, will the Court vacate an order of the Commission solely on the grounds that in appellants' judgment, different conclusions might have been reached upon evidence before the Commission.

## INDEX

### SUBJECT INDEX

	<u>Page</u>
Questions Presented.....	i
Counterstatement of the Case .....	1
Summary of Argument .....	6
Argument:	
I <u>The present appeal is moot in view of the fact that the order appealed from has been superseded by a subsequent rate order</u> .....	9
II <u>Appellants can point to no error of law in the Commission's Order. The numerous allegations of error expressing a position contrary to that taken by the Commission is an attempt to substitute the appellants' judgment for that of the Commission.</u> .....	13
A.   The Gross Operating Revenue Base .....	14
B.   The Rate Base .....	15
C.   Accounting .....	19
D.   Fair Return .....	26
Conclusion .....	31
Appendix 1:	

Statement of Congressman Harris on proposed bill to restore Franchise to Capital Transit Company.

#### Appendix 2:

Statement of Congressman Harris in re S 3070 (D. C. Transit, System, Inc. Franchise).

# CASES CITED

	<u>Page</u>
<u>Alabama Power Co. v. F. P. C.</u> , 75 U.S. App. D. C. 315, 128 F 2d 280 (Cert. den. 317 U.S. 652, 63 S. Ct. 48, 87 L. Ed. 525) .....	24
<u>American Tel. &amp; Tel. Co. v. U. S.</u> , 299 U. S. 232, 236-237, 57 S. Ct. 170, 81 L. Ed. 178.....	25
<u>Arkansas Power &amp; Light Co. v. F. P. C.</u> , 87 U. S. App. D. C. 385, 185 F 2d 751 (Cert. den. 341 U. S. 909, 71 S. Ct. 621, 95 L. Ed. 1346) .....	24
<u>City of Detroit v. F. P. C.</u> , 97 U. S. App. D. C. 260, 230 F 2d 810 .....	15
<u>Clarion River Power Co. v. Smith</u> , 61 App. D. C. 186, 59 F 2d 861 (Cert. den. 287 U. S. 639, 53 S. Ct. 88, 77 L. Ed. 553) .....	24
<u>D. C. Transit System, Inc. v. P. U. C.</u> , 292 F. 2d 734, _____ U. S. App. D. C. _____ .....	17, 25
<u>F. P. C. v. Hope Natural Gas Co.</u> , 321 U. S. 591, 88 L. Ed. 333, 64 S. Ct. 281 .....	31
<u>Kansas City So. Ry. v. U. S.</u> , 231 U. S. 423, <sup>456</sup> <del>238-237</del> , 34 S. Ct. 125, 58 L. Ed. 296 .....	25
<u>Los Angeles Gas and Electric Corp. v. Railroad Commission</u> , 289 U. S. 287, 53 S. Ct. 637, 77 L. Ed. 1180 .....	16
<u>Norfolk &amp; Western R. R. Co. v. U. S.</u> , 287 U. S. 134-141, 53 S. Ct. 52, 77 L. Ed. 218 .....	25
<u>Northwestern Electric Co. v. F. P. C.</u> , 321 U. S. 119-124, 64 S. Ct. 451, 88 L. Ed. 596 .....	24
<u>Potomac Electric Power Company v. P. U. C. et al</u> , 81 U. S. App. D. C. 225, 158 F 2d 521 (Cert. den. 67 S. Ct. 1303, 331 U. S. 816, 91 L. Ed. 1834) .....	15



	<u>Page</u>
Re D. C. Transit System, Inc. 38 PUR 3d, 19 .....	2, 10
Re D. C. Transit System, Inc. 25 PUR 3d 371 .....	26
<u>U. S. v. P. U. C., et al</u> , 81 U.S. App. D.C. 237, 158 F 2d 533 (Cert. den. 67 S.Ct. 1305, 331 U.S. 816, 91 L.Ed.1835) .....	15

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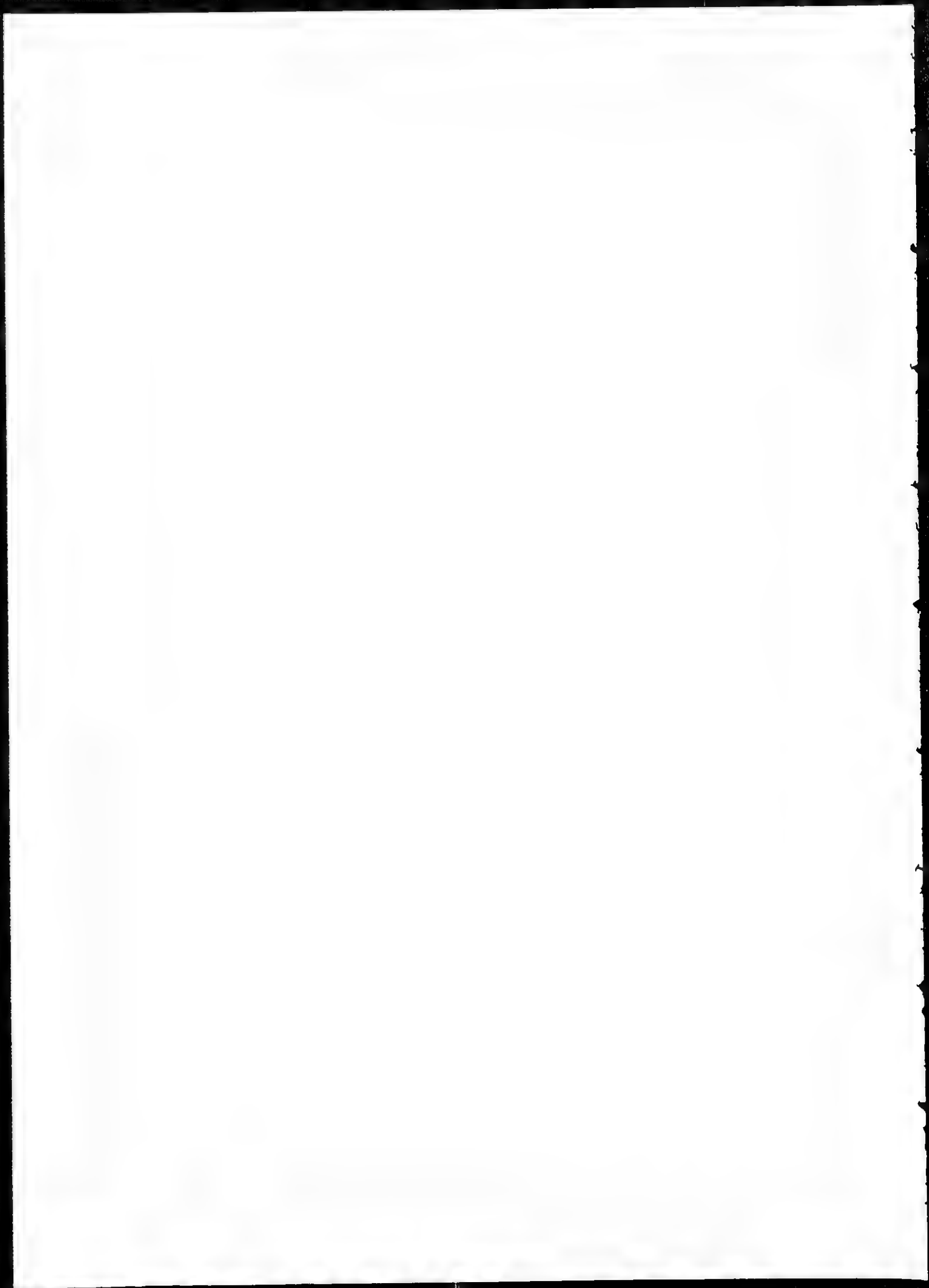
D. C. Code, 1951 edition:	
Sec. 43-707, Par. 67 .....	11
Sec. 43-709, Par. 69 .....	11
Public Law 435, 62nd Congress, 37 Stat. 974, March 4, 1913 .....	11, 24
Public Law 757, 84th Congress, 70 Stat. 974, July 24, 1956:	
Sec. 4.....	14, 26, 27, 29, 30
Sec. 5 .....	26, 28
Public Law 794, 86th Congress, 74 Stat. 1031, September 15, 1960 .....	2, 12, 15

#### OTHER AUTHORITIES

43 Am. Jur., Public Utilities and Services Par. 105 .....	16
--	----

#### MISCELLANEOUS

102 Congressional Record 8292, May 16, 1956 .....	18, 24, App.1
102 Congressional Record 13580, July 19, 1956 .....	18, App. 2
Committee Report to accompany S 1745, Calendar No. 857, 87th Congress, dated September 15, 1961.....	30, 31



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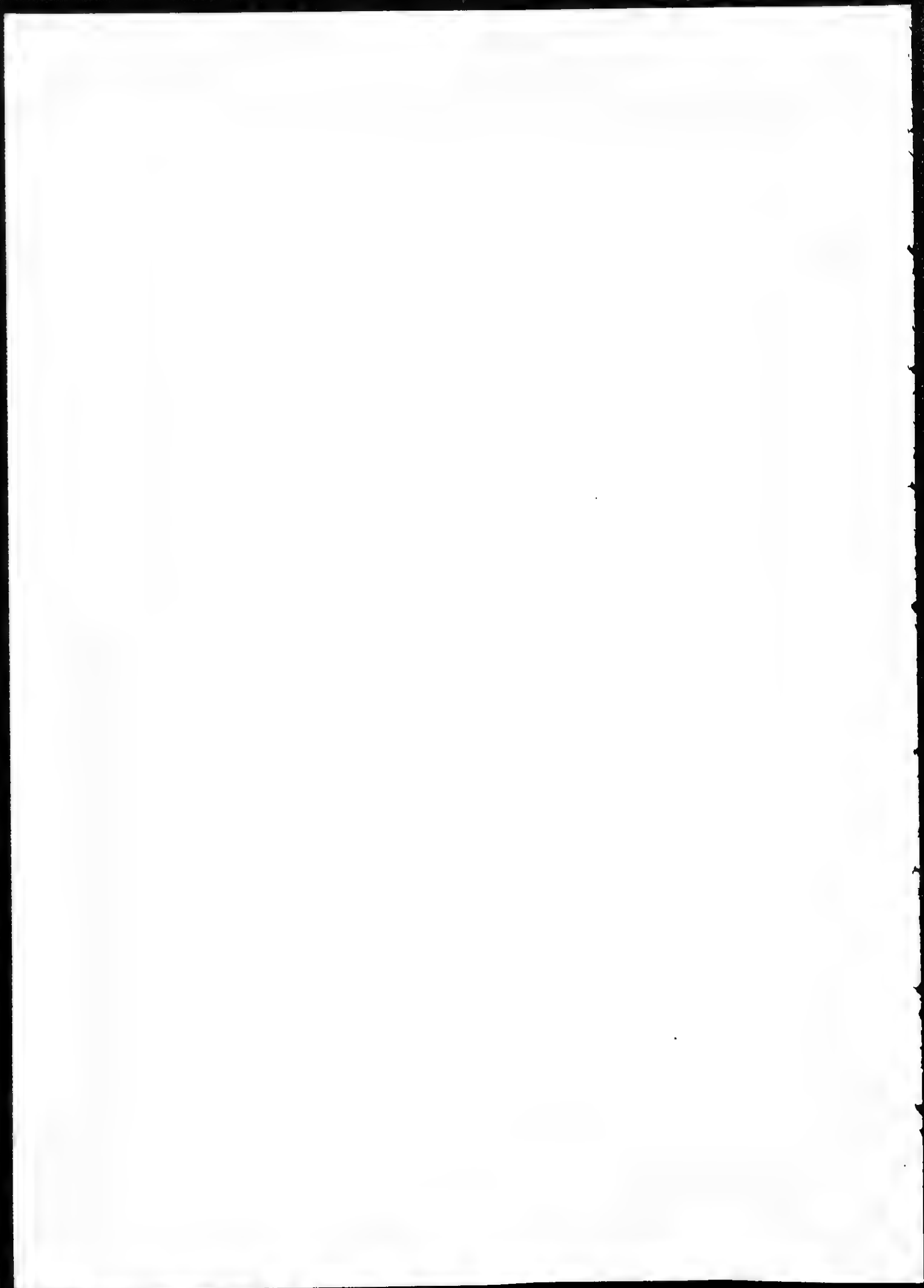
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BRIEF FOR APPELLEE PUBLIC UTILITIES COMMISSION

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COUNTERSTATEMENT OF THE CASE

Appellants' statement of the case contains matters having no bearing on this appeal and does not mention two matters which have happened subsequent to the entry of the order in this case which the appellee commission considers important. The two matters (referred to in the body of the brief of appellants) are that D. C. Transit System,



Inc. (Transit) subsequently filed on September 14, 1960, another petition with the Commission for a change in its schedule of rates, and the Commission, after full hearing issued its Order No. 4735 on January 18, 1961 (38 PUR 3d 19). Secondly, the Washington Metropolitan Area Transit Commission (WMATC), pursuant to Public Law No. 86-794, 86th Congress, approved September 15, 1960, assumed jurisdiction of passenger carriers in the Washington Metropolitan Area on March 22, 1961, which carriers include Transit.

This is a statutory appeal from Order No. 4631 of the Public Utilities Commission (Commission) determining the schedule of rates to be charged within the District of Columbia by Transit. The certified record filed with the Court shows that formal public hearings were held by the Commission on Transit's petition for a change in its schedule of rates for eleven days during the period, November 11, 1959 to February 19, 1960, inclusive, resulting in a record of 2077 pages and 96 exhibits.

The record made before the Commission, its Findings, Conclusions, Order and Opinion based upon that record, together with the petitions for reconsideration and the order entered thereon, and the order of the District Court dismissing the appeal and affirming the Commission's order, constitute the record before the Court.

Perhaps the most appropriate way to present the case in its proper perspective is to quote from the Commission's Order No. 4645

denying petitions for reconsideration filed by the appellants on the one hand and Transit on the other. The Commission stated, (Certified Record), inter-alia :

"The Commission has before it two petitions for reconsideration of its order in the above-titled proceeding both filed on April 1, 1960. .. The two petitions are diametrically opposed in content and approach to the issues raised in the rate case.

The petition of the District of Columbia Federation of Civic Associations, American Federation of Government Employees (Counsel of Defense Lodges and District of Columbia Department), Friendship Citizens Association, Ralph E. Hays, Thomas G. Harris, Paul Seligson, Henry W. Thomas, Leonard S. Dwor, Leonard S. Goodman, Leonard N. Bebachick, George I. Obate, George Spiegel, and Barrington D. Parker, contains 47 allegations of error. In the aggregate, and in substance, they reflect the petitioning group's view that the Company was not entitled to any change in the pre-existing authorized fare structure.

In considering this petition, we find it impossible to reconcile the position taken by the petitioners with the demonstrated needs of the Company. As a practical matter, by the purchase of five tokens for \$1.00, they experience no increase in fares under the fare structure authorized in this proceeding.

On the other hand, the petition for reconsideration filed by D. C. Transit System, Inc., alleges numerous errors made by the Commission, which it contends, in the end result, fail to give the Company the return to which it is entitled. Its conclusion, based on this assumption, is that the Commission



should have approved the two fare structures initially requested by the Company, or, alternatively, should have approved a subsequent fare structure submitted by the Company during the course of the rate proceeding.

In considering this petition, we also find it impossible to reconcile what we consider to be excessive demands of D. C. Transit System, Inc. with the right of the rate payers to the lowest possible fares consistent with a fair return to the Company.

We have carefully reviewed the record and our order entered in this proceeding in light of the subject petitions for reconsideration. The petitions are mutually exclusive, and, obviously, if either approach used is the correct one, the other must be wrong. Fair return is an area, not a line or a point, and our discretion must be exercised with a view to the public interest, consistent with the needs of a financially sound transit system, or, as we have said so often, there must be a fair and reasonable balancing of investor and customer interests. We believe, and we so indicated in our Order No. 4631, that there is an area of reasonableness falling between the extremes indicated by these two petitions for reconsideration. No purpose would be served in reiterating the basic reasons for the decision made and promulgated in this case. The order and opinion in support thereof speak for themselves, and we find nothing in the petitions for reconsideration which would warrant findings and conclusions different from those reflected in said order of March 2, 1960. "

As a consequence, the Commission denied the petitions for reconsideration and, although the Citizens' Groups have not pursued the matter further, the present appellants among others appealed to the

Court below. Transit filed a separate appeal from the Commission's order which has been terminated favorably to the Commission.

The District Court after full consideration, denied appellants' motion for summary judgment, dismissed the appeal and affirmed the Commission's order (JA 39-41). Thereafter appellants filed their Notice of Appeal (JA 42).

SUMMARY OF ARGUMENT

Appellee Commission contends that a subsequent rate case initiated by Transit, and the order and opinion of the Commission promulgated pursuant thereto supersede the order appealed from, and renders the present appeal moot. If, however, this Court should find that the present appeal is not moot, then the District Court's order affirming the Commission's order and dismissing appellants' complaint should be affirmed for the reasons stated therein. Appellants' numerous allegations of error merely constitute differences of opinion with that of the Commission. Where appellants attempt to interpret the law, such interpretation finds no support in the record and action by the Congress when dealing with the identical subject matter can only be interpreted as recognition and approval of the regulatory action taken by this Commission.

The Commission utilized the gross operating revenue base method to fix rates for Transit in this case in accord with the admonition of the Congress that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible.

The rate base found by the Commission was arrived at on the basis of actual amounts recorded on the books of Transit with appropriate adjustments. Net investment based on original cost and the

net investment based on purchase price were both found by the Commission to be proper elements of value for consideration and were given equal weight in determining a system rate base for the purpose of this proceeding. Appellants' contention that the Commission should have ignored that element of value represented by net investment based on original cost cannot be sustained.

The basic act under which the Commission operates, confers broad discretion upon the Commission in regulating the accounting procedure of utilities under its jurisdiction. Appellants have not shown, nor can they show that the accounting authorized by the Commission is unreasonable, arbitrary or capricious, or that such accounting is erroneous as a matter of law.

What constitutes a fair return to a utility is a question of fact to be determined by the regulatory body. Fair return is an area, not a line or a point and the Commission's discretion, under recognized standards and rules, has been exercised by reasonably balancing the interests of the public consistent with the needs of a financially sound transit system. While the return on equity permitted Transit might be considered generous under some circumstances, it is entirely consistent with the Franchise under which it operates and with the treatment afforded Transit by the Congress. Certainly the 4.10% return on gross operating revenues permitted by the Commission in

this case falls well within the 6 1/2% return on gross operating revenues which the Congress declared in Transit's Franchise would not be unreasonable.

The end result of the Commission's rate order is that, in spite of inflation and increased costs and expenses of operation amounting to hundreds of thousands of dollars annually, the majority of riders in the District of Columbia are still enjoying a 20¢ fare for public transportation. Neither Transit nor the public can reasonably complain of results such as these.

## ARGUMENT

### I

The Present Appeal Is Moot In View Of The  
Fact That The Order Appealed From Has  
Been Superseded By A Subsequent Rate Order

Sumarized, it is the contention of appellee commission that a subsequent rate case involving Transit, and the Order and Opinion promulgated pursuant thereto, superseded the order appealed from and renders the present appeal moot. Very briefly, the sequence of events leading to this conclusion are:

This appeal is from an order of the United States District Court for the District of Columbia entered June 5, 1961, affirming Order No. 4631 of the Commission. Order No. 4631 and the Commission's opinion in support thereof were promulgated after extended public hearings initiated by Transit with the filing on November 6, 1959, of a petition for a change in its schedule of rates. On the basis of the evidence in the case, the Commission rejected the schedule of rates requested by Transit on the ground that the same were excessive and unwarranted, but gave some rate relief in the form of an increase in cash fare from 20¢ to 25¢.<sup>1</sup>

Transit and appellants in separate actions in the District Court (C. A. No. 1439-60 and C. A. 1529-60) appealed from the order of the

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<sup>1</sup>/ The rate order retained the existing token fare of 20¢ (5 for \$1.00).



Commission. From adverse decisions, both appealed to this Court. Transit's case (16107) was subsequently dismissed and there remains only the present appeal from Order No. 4631.

Meanwhile, on September 14, 1960, Transit filed a new petition with the Commission for a change in its schedule of rates. Formal public hearings were held on thirteen days during the period from September 29, 1960 to January 4, 1961, inclusive, resulting in a record consisting of 2,014 pages and 74 exhibits. On the basis of evidence there adduced, the Commission on January 18, 1961, issued its Order No. 4735<sup>2</sup> denying the requested increase in the schedule of rates filed by Transit; concluding that the then existing schedule of rates consisting of 25¢ cash fare, tokens at 5 for \$1.00 and a 10¢ school fare was, under the circumstances of that case, just, reasonable, and compensatory, and would enable the Company to meet its obligations, maintain a sound financial structure, reasonably compensate investors and enable the Company to furnish adequate service (38 PUR 3d, 19).

Subsequently, the Commission denied two petitions for reconsideration of Order No. 4735, and two separate appeals were filed in the District Court of the United States for the District of Columbia. Leonard N. Bebachick, appellant here, took an active part in the hearings and is a party to one of the appeals (C. A. No. 825-61). This appeal is now

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<sup>2/</sup> The opinion in support thereof was issued February 27, 1961.

pending in the District Court.

As a matter of law, the Congress has limited the duration of the effectiveness of the Commission's orders and decisions by providing in Par. 67 of the basic law,<sup>3</sup> Sec. 43-707, D. C. Code, 1951, that "All orders and decisions of the commission shall remain in full effect, \*\*\* unless and until they are suspended, superseded, or recinded by the commission. \*\*\*\*" It follows that as a consequence of the order entered in the subsequent rate case, Order No. 4631 has been superseded and is therefore moot.<sup>4</sup>

Assuming, arguendo, that this Court might sustain one of the numerous allegations of error advanced by appellants, appellee contends that such action could not effect the Commission's subsequent rate Order No. 4735 entered on the basis of a new record made in a new rate proceeding.

In their motion addressed to this Court of July 6, 1961, appellants, in effect, request this Court to render an advisory opinion in this case since they stated, inter-alia, on Page 4:

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3/ For the convenience of the Court, Public Law 435, approved March 4, 1913 (37 Stat 974) Sec. 8 of which creates the Public Utilities Commission, will be referred to by paragraph (Par.) and the corresponding citations, Title 43, D. C. Code, 1951, will be referred to by Section (Sec.).

4/ In passing, it may be noted that the Commission may by statute, recind its orders at any time, even after appeal is filed. Par. 69, Sec. 43-709. Circumstances, rather than the Commission action, resulted in recision of Order No. 4631. The end result is identical.

"Further, it is likely that Transit will petition the Metropolitan Area Transit Commission, successor to appellee Commission, for a further increase in fares in the near future. Many of the issues here raised by appellants will be highly relevant to a just determination of future rate proceedings. A prompt adjudication of this appeal will facilitate the just and efficient functioning of the administrative process and will serve to lessen the need for further litigation. \*\*\*" <sup>5</sup>

While appellee Commission cannot concede that a proper function of this Court is to render advisory opinions for the benefit of a non-litigant administrative body, it does not press the point since a decision on the merits (advisory or otherwise) might well serve to end once and for all the chimerical approach of appellants to utility regulation.

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<sup>5/</sup> The Washington Metropolitan Area Transit Commission pursuant to Public Law 86-794, 86th Congress (Compact), approved September 15, 1960, assumed jurisdiction over carriers in the Washington Metropolitan Area on March 22, 1961.

## ARGUMENT

### II

Appellants Can Point To No Error Of Law In  
The Commission's Order. The Numerous  
Allegations Of Error Expressing A Position  
Contrary To That Taken By The Commission  
Is An Attempt To Substitute The Appellants'  
Judgment For That Of The Commission.

The appellants' statement of points, separated into eighteen paragraphs alleges the Commission erred in the order appealed from and in the opinion in support thereof, with respect to practically every issue contested before the Commission in its hearing on the rate case. Apparently, appellants have abandoned the position taken before the District Court that these were errors of law (cf. complaint, JA 32-37, and order of the District Court disposing of motion for summary judgment, JA 39-41). A fair reading of appellants' statement of points and arguments in support thereof demonstrates that in the aggregate and in substance, they constitute nothing more than an effort on the part of the appellants to control and direct the exercise of the administrative discretion lodged in the Commission by the Congress. To establish some order in its presentation, appellee commission will attempt to divide its brief into sections to answer appellants' allegations as it understands them.

A

The Gross Operating Revenue Base

Appellants claim that the Commission erred in concluding that the gross operating revenue method should be utilized to fix transit rates. The Commission discussed this aspect of the case at length in its opinion in support of its findings, conclusion, and order (JA 5-11). This included not only a factual discussion of the administrative steps taken by the Commission in furtherance of the legislative policy enunciated by the Congress in Sec. 4 of the Franchise Act (Appendix A, appellants' brief) but also the implications flowing therefrom. Without repeating the Commission's reasoning, it is sufficient to say that the Commission ultimately concluded that the gross operating revenue method should be utilized to fix rates for Transit. Presumably, appellants would have the Commission, and would now have this Court adopt the position of an "expert" witness, who had not even read Transit's Franchise (JA 176) and who opposed the theory of the gross operating revenue method of rate making because he did not consider such a method would be proper or warranted under any conditions (JA 192). Apparently, appellants still do not recognize that the Commission is an agency of the Congress, and would have the Commission disregard the admonition of Congress "that the Commission should encourage and facilitate the the shifting to such gross operating revenue base as promptly as possible and as conditions warrant; and if conditions warrant not later than

August 15, 1958. " <sup>6</sup> Appellants' contentions in this respect can only be branded as frivolous.

B

The Rate Base

Bearing in mind that the rate base found by the Commission was only for the purpose of testing the reasonableness of a return computed under the gross operating revenue method (See City of Detroit v. F. P.C. 97 U. S. App. D. C. 260, 230 F 2d 810) the attack by appellants on the Commission's rate base is incomprehensible. This Court has held that the statute does not undertake to provide a formula for determining rates and that if a fair return is established, irrespective of the method followed, there is no ground for complaint. This Court has also held that the statute does not condition rate-making upon valuation. Potomac Electric Power Company v. PUC, et al, 81 U. S. App. D. C. 225, 158 F 2d 521 (Cert. den. 67 S. Ct. 1303, 331 U. S. 816, 91 L. Ed. 1834), and U. S. v. PUC, et al, 81 U. S. App. D. C. 237, 158 F 2d 533 (Cert. den. 67 S. Ct. 1305, 331 U. S. 816, 91 L. Ed. 1835). That the courts have consistently refused to interfere with the method used by administrative bodies is succinctly

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<sup>6</sup> / It is noteworthy that the Congress in granting its consent and approval to the Compact, supra, relating to transportation in the Washington Area, refers only to a return in terms of gross operating revenues. Title II, Sec. 6 (a), (4).



stated by Chief Justice Hughes in Los Angeles Gas and Electric Corp. v. Railroad Commission, 289 U. S. 287, 53 S. Ct. 637, 77 L. Ed. 1180, when he said:

\*\*\*\*The legislative discretion implied in the rate-making power necessarily extends to the entire legislative process, embracing the method used in reaching the legislative determination as well as that determination itself. \*\*\*\*" (Page 304, Emphasis supplied).

Historically, the methods used for ascertaining rate base (valuation for rate-making purposes) may be divided into three general categories: (1) original cost depreciated, sometimes called book value; (2) present value of the property; and (3) reproduction cost. Notwithstanding that some jurisdictions may use one or the other of these methods to the exclusion of the others, it is recognized that valuation for rate-making purposes cannot be solved by a formula applicable to all circumstances but must depend upon particular circumstances and factors affecting particular utilities when their rates are called into question (43 Am. Jur., Public Utilities and Services, Par. 105).

The reason that no formula is applicable to Transit is apparent. The original cost, less accumulated depreciation, of the properties of Capital Transit Company when Transit acquired them adjusted to date, is in the area of \$19,000,000 (JA20). The purchase price as adjusted, is approximately \$13,000,000 (JA 20). The appellants' argument in at

least one segment of their brief is that the purchase price is the maximum proper rate base (Statement of Points No. 11).<sup>7</sup> This of course does not follow, and the inapplicability of such a method of valuation may be easily demonstrated. Assuming the identical \$19,000,000 book value and a purchase price of \$25,000,000, must it necessarily follow that rate base would then be \$25,000,000? An even more unlikely assumption, i. e., with the identical \$19,000,000 of book value, and a donation (for whatever reason) of the properties, does it follow that an acquiring company is entitled to no rate base at all? The questions answer themselves.

Admittedly, D. C. Transit acquired the properties of Capital Transit for approximately \$10,000,000 less than the book value of the property. Subsequent events have shown that the purchase price would not necessarily represent the value. Certain properties disposed of by the present owner, Transit, sold for almost three times original cost, as distinguished from book value. The order directing accounting for proceeds from sale by Transit of its Fourth Street Shop and Southern Carhouse Properties (Order No. 4577), was reviewed by this court, 292 F 2d 734, \_\_\_\_ U. S. App. D. C. \_\_\_\_\_. This transaction in and of itself would appear to indicate the danger of accepting what amounted to a "forced sale price" as the sole criteria for rate base.

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<sup>7/</sup> This is, however, only one point in a scatter-shot approach to the subject. In their brief appellants contend: a rate base valuation of about \$12.5 million is fair and reasonable, (p 53); that \$9.2 million is a maximum limit rate base (p 57); and that a proper rate base would be under \$6.4 million (p 57).

The Commission in discussing its rate base determination (JA 19-23) found that both the net investment based on original cost and the net investment based on purchase price were proper elements of value to be considered in determining a system rate base for purposes of this proceeding. It further noted that all of the elements of value considered were based on actual amounts recorded on the books of Transit with appropriate adjustments (JA 22). Appellants insist that no element of value other than purchase price should be considered. Thus, notwithstanding the fact that the Congress has not legislated,<sup>8</sup> and the Courts have refused to impose their views upon administrative bodies on what is essentially a factual determination, appellants here seek to impose upon the Commission a method or formula for rate base amounting to an infringed rule of law of their own making.

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<sup>8/</sup> In addition to the Committees of Congress consistently requiring reports from the Commission on actions taken, the Congress is kept fully informed of Commission actions through the medium of annual reports to that body. See Appendix 1 to illustrate the familiarity of Congress with the Commission's depreciation practices and rate base methods and Appendix 2 indicating why the Congress did not set a rate base in Transit's Franchise.

C

Accounting

The Commission in its order discusses the accounting treatment applicable to depreciation, amortization of acquisition adjustment, and provision for track removal and repaving (JA 12-18). This section of the order deals with those matters which appear to particularly displease appellants. While appellee Commission does not pretend that it can follow the devious reasoning of appellants in all respects (See footnote 7, supra, for example), a review of the record and appellants' brief leads to the inescapable conclusion that a fundamental error permeates the entire approach of appellants to this case. They are apparently wedded to the proposition, advanced by their witness, that on or about August 15, 1956, the rail properties devoted to public transportation in the District of Columbia became valueless (JA 16).

The record shows, inter-alia, that Transit's gross operating revenues derived solely from its rail system operation, amounted to more than \$12,000,000, \$11,000,000, and \$10,000,000 in 1957, 1958, and 1959 respectively (JA 239). The Commission rejected appellants' approach of "no value" by stating (JA 16), "We fail to see how rail facilities could be considered as valueless when they had a remaining useful life of seven years and were at the time producing annual revenues

of approximately \$12,000,000."

Separate and apart from the Commission's rejection of the theory that the rail properties were valueless, it is impossible to reconcile appellants' position with the actual facts existing at the time Transit took over the local transportation system. Certainly no rational argument may be advanced which could convince the users of public transit that the rail system had become valueless over-night. Exactly the same facilities were available to transit riders under operation by Transit as were available under operation by its predecessor.

In spite of a great deal of conflicting testimony by appellants' witness,<sup>9</sup> he finally conceded that if the acquisition adjustment was applied against Transit's property in order to value the assets at their purchase price, depreciation would be provided on the basis of purchase price and Transit would then have to accrue for the coverage of its liability to remove the tracks and to repave (JA 222).

To appellee this represents a full acceptance by the witness of the Commission's treatment of the acquisition adjustment in using it as an off-

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<sup>9/</sup> This witness not only testified that the rail properties were valueless, supra; he also testified that rail properties represented assets of some \$10 million contributed by the predecessor company (JA 219-220); that the rail properties had a remaining value of \$5,121,000; and that the fare payers had already borne the burden of loss of rail values and the cost of track removal and repaving (JA 224) with an immediate retraction of the latter statement and a denial that Transit riders had borne any part of this expense (JA 225).



set to depreciation on original cost, thus effectively reducing depreciation to the basis of purchase price, and separately providing for cost of track removal and repaving (details set out in Commission's Order (JA 12-18)).

The same result logically follows if the acquisition adjustment of approximately \$10,000,000 is treated as a reserve or liability for track removal and repaving (App. Br. 26), for it must then be added as any other liability or reserve to the purchase price so that the purchase price of the property is the depreciated original cost of approximately \$19,000,000 as of August 15, 1956 adjusted by giving effect to changes in various accounts to a total depreciated cost of \$19,141,507 as of September 30, 1959 (Sched 4, Ex. 39, JA 53). Depreciation would then be accrued on Transit's cost (purchase price) without offset and without provision for track removal, thus achieving substantially the same end result attained from the Commission's accounting requirements.

The appellants' contentions with respect to the provision being made by the Commission for track removal and repaving costs (App. Br. P. 18, 22, and 23) deserve little comment. At the time of the hearing, the best information available was that it would cost approximately \$10,000,000. The Commission is providing for this amount in equal installments over a ten-year period, subject however to continuing study for appropriate adjustment when and if justified.

There is no definite schedule for track removal and repaving,



although Transit's liability therefor is fixed by law. It is possible that costs may vary from a few thousands in one year to several million in another, and it would be impractical to attempt to fix rates to recover these costs as they are incurred. The Commission's provision of an equal annual charge is a practical and reasonable method of providing these future costs and inures to the benefit of both the riding public and the company, with control thereover retained by the Commission. Appellee is unable to follow appellants' contention that the provision should be adjusted for tax effect. The record shows that Transit has claimed the provision for track removal as a deduction for tax purposes, thereby reducing the amount of income taxes charged as an expense against the customers.

Appellee likewise cannot follow appellants' argument that expenditures for track removal are a proper basis for increasing the rate base above purchase price (App. Br. 47). They refer to this as an increase in investment to be recovered through depreciation or increased return, but fail to tell us what property represents this increased investment and what property is to be depreciated in the future to recover this investment. The only significance we can attach to this is that while appellants heretofore claimed that the stockholders should pay for the cost of track removal (App. Br. 19), they now recognize track removal costs as a proper expense to be recovered by Transit.

Finally, appellants contend the Commission erred in allowing unlawful depreciation on certain rail properties and buses (App. Br. 24, et seq). The Commission fully discusses the prescribed accounting in its Order (JA 14-15) and its reasons for taking the conservative approach it did in allowing for the extraordinary retirement loss relating to only part of the track facilities.

With reference to buses, under then existing orders, depreciation was provided for on a "group basis". Under this method, property is treated as a group rather than as individual units and no portion of the depreciation reserve is associated with any particular part of the property. The group method has been followed by the Commission for many years, and is followed by many other regulatory bodies as well. Under this method, depreciation rates are based on an average service life for a particular class of property, and accruals on property extending beyond the normal retirement date are assumed to offset under-accruals on premature retirements. The staff did not recommend any change in this procedure. The staff's studies (made on a unit basis) from which the \$1,200,000 figure was developed, was used by the staff only to point out that accrued depreciation on over-age buses might be available to some extent to offset extraordinary retirement losses on rail facilities claimed by Transit.

Appellants on the other hand would retroactively apply the "unit"

method with respect to buses, without the benefit of a depreciation study to determine the adequacy of the depreciation reserve with respect to other classes of property. As stated before, the Commission did not adopt appellants' views, either as to bus depreciation or in making provision for extraordinary retirement loss related to the retirement of rail facilities having a remaining undepreciated cost of over \$2,500,000. This action of the Commission is entirely compatible with the intention of Congress as evidenced by the statements of Congressman Harris when discussing the identical property (Appendix 1).

Throughout the basic act creating the Public Utilities Commission, constant reference is made to the Commission's right as well as to its duty to supervise and control the accounting practices of public utilities under its jurisdiction. Where accounting matters are committed to administrative bodies, the courts have consistently refused to determine accounting practices or interfere with accounting requirements unless the administrative body has "plainly adopted an obviously arbitrary plan." Northwestern Electric Co. v. F. P. C., 321 U. S. 119, 124, 64 S. Ct. 451, 88 L. Ed. 596. Arkansas Power and Light Co. v. F. P. C., 87 U. S. App. D. C. 385, 185 F 2d 751, (Cert. den. 341 U. S. 909, 71 S. Ct. 621, 95 L. Ed. 1346); Alabama Power Co. v. F. P. C., 75 U. S. App. D. C. 315, 128 F 2d 280 (Cert. den. 317 U. S. 652, 63 S. Ct. 48, 87 L. Ed. 525); Clarion River Power Co. v. Smith, 61 App. D. C. 186, 59 F. 2d. 861,

(Cert. den. 287 U. S. 639, 53 S. Ct. 88, 77 L. Ed. 553). In attacks upon administrative accounting orders, the courts have said that even though they were in disagreement with the regulatory agency "as to the wisdom and the propriety of the order, we are without power to usurp its discretion and substitute our own." Norfolk & Western R. R. Co. v. U. S., 287 U. S. 134, 141, 53 S. Ct. 52, 77 L. Ed. 218; see to the same effect Kansas City So. Ry. v. U. S., 231 U. S. 423, 456, 34 S.Ct. 125, 58 L. Ed. 296; American Tel. & Tel. Co. v. U. S., 299 U. S. 232, 236-237, 57 S. Ct. 170, 81 L. Ed. 178.

The District Court concluded that the findings of the Commission were not unreasonable, arbitrary, or capricious, and that its conclusions and decision were not erroneous as a matter of law (JA 41). In D. C. Transit System, Inc. v. Public Utilities Commission, 292, F 2d. 734, U.S. App. D. C. \_\_\_\_\_, this Court stated:

"Sections 43-310 and 43-314, D. C. Code (1951), confer broad discretion upon the Public Utilities Commission in regulating the accounting procedures of utility companies under its jurisdiction. Our function in reviewing the Commission's orders and decisions is limited to questions of law including constitutional questions; and the Commission's findings of fact are conclusive unless it appears that the findings are unreasonable, arbitrary, or capricious. D. C. Code §43-706 (1951). We find no error on the part of the District Court in determining that the Commission's order of September 30, 1959, was not unreasonable, arbitrary, or capricious. We see no constitutional question involved."

Appellee Commission believes the above statement equally applicable to the conclusions reached by the District Court in its order entered on this appeal.

D

Fair Return

Throughout the brief of appellants they speak of excessive earnings by Transit (App. Br. 16); the capital attraction standard prescribed by the Franchise (App. Br. 37); the intention of Congress that Transit should earn only that return needed to attract capital on favorable terms, described as its cost of capital (App. Br. 39); that the Congress prescribed as an ultimate standard the setting of rates sufficient to cover expenses and attract capital (App. Br. 61) and that the statute (Sec. 4 of the Franchise) requires rate-of-return-on-rate-base method of rate making to gauge the fairness and reasonableness of Transit's income as a percentage of its net investment (App. Br. 62). This is pure nonsense. The record of Transit's operations from August 15, 1956 to November 6, 1959 (the date when the present proceedings were initiated by Transit's new schedule of rates) shows conclusively that the rates Transit was permitted to charge in the District of Columbia were in large part, those rates applicable to the predecessor company (Sec. 5 of the Franchise, *infra*). The first order issued by the Commission affecting Transit's rates became effective September 1, 1958 (Re D. C. Transit System, Inc. 25 PUR 3d



371). It follows that for two of the approximately three years of Transit's operations prior to the present proceeding, it was the Congress rather than the Commission which controlled the schedule of rates.

If, as appellants would have this Court believe, Transit's earnings have been excessive, the Congress was in large part responsible. If Sec. 4 of the Franchise is a mandate from the Congress for this Commission to gear "rate of return" to "a particular rate base" or to "cost of capital," the Congress certainly saw fit to deliberately ignore that "mandate" during that period when it directly exercised the rate-making power over Transit. Obviously the Congress made no effort to equate the rates authorized with either the cost of capital or a particular rate base. Indeed, if anything adoption of the rates applicable to the predecessor company show a clear intention on the part of Congress that Transit, regardless of the terms on which it acquired the transportation facilities in the District of Columbia, should fare no worse in terms of revenue than its predecessor.

The Commission discussed in its opinion its Determination of Fair Return (JA 23-27). Appellants' complaint about what they regard as an excessive return of 30% on Transit's total equity investment is intermixed with an allegation that Transit has been permitted to annually pay its stockholders dividends at the rate of 100% of their present capital stock investment (App. Br. 16). Even if true,<sup>10</sup> the reference to annual 10/ Appellants own Exhibit (JA 65) shows only an average annual yield of 66.4%.



dividends of 100% on original capital investment would have no significance, since retained earnings and the profit on the sale of its southwest property in excess of \$2,000,000 also constitutes equity invested in the company. The 30% return on equity capital must be considered in the light of the small percentage of equity in Transit's capital structure and the fact that this Commission had no control of the capital structure of Transit when it acquired and began to operate a transportation system in the District of Columbia. It is appropriate to note that the Congress in Section 5 of the Franchise fixed the rates of the company for a time certain to continue in effect until August 15, 1957, and thereafter until superseded by a new schedule of rates. The specific language in Section 5 is:

"The initial schedule of rates which shall be effective within the District of Columbia upon commencement of operations by the Corporation shall be the same as that effective for service by Capital Transit Company, \*\*\* in effect on the date of the enactment of this Act and thereafter until superseded by a schedule of rates which becomes effective under this Section."

By virtue of this and other provisions of the Franchise combined with the lean equity mentioned above, Transit has indisputably been enabled heretofore, to earn a return on its equity in excess of the 30% appellants here complain of.

Equally misleading is appellants' claim that through excessive fares Transit "has paid off millions of dollars of short term debt obliga-

tions" (App. Br. 16-17). The record shows that cash realized from the sale of Transit's southwest property, cash in the company upon acquisition, and cash generated through provision for depreciation were the principal sources of funds for paying off debt (JA 115). To appellee Commission expenditures of cash on hand to lower interest expenses represents prudent management on the part of Transit.

As stated above the Commission fully discussed its determination of a fair return for Transit under the circumstances of the case. Included in this discussion was a consideration of the evidence and testimony of the various witnesses pertaining to the subject matter. After consideration of all of the facts, the Commission concluded that net operating income of \$1,143,249 for the twelve months ending December 31, 1960 resulting from the District of Columbia fare structure approved, would enable Transit to meet its interest requirements, pay reasonable dividends, permit retention of a reasonable proportion of earnings in the business, provide a margin for unforeseen contingencies and enable the company to attract the necessary capital to meet its future capital requirements (JA 27).

In the course of its discussion, the Commission noted that what constitutes a reasonable return is a question of fact and that there is no established legal precedent on any economic formula which may be universally applied in the determination of a proper rate of return. The Congress has stated in Section 4 of the Franchise that Transit should be entitled to a

return in accordance with standards and rules prescribed by the Commission. Once having determined a fair return in accord with its standards and rules under just and reasonable rates (which rates in this particular case would yield 4.10% return on gross operating revenues) the Commission (and the Court) does have a statutory rule of thumb by which the reasonableness of the return allowed can be measured.

Applying the declaration of legislative policy in Section 4 of the Franchise that "the Congress finds that the opportunity to earn a return of at least 6 1/2 per centum, \*\*\*on gross operating revenues would not be unreasonable, \*\*\*" to the 4.10% return on gross operating revenues permitted by the Commission in this case, can lead to but one conclusion. The return allowed is well within the bounds of reasonableness set by Congress.

Notwithstanding that appellants purport to speak for the Congress, the uncontrovertible fact is that Committees of the House and Senate, with full knowledge of the Commission's treatment of Transit on rate of return favorably considered and reported out companion bills in the last session which would principally benefit Transit. S. 1745 was passed by the Senate on September 26, 1961. The bill, designed as a means of providing affected carriers with payments, in the form of a subsidy, to compensate them for half-fare rates levied by law on school children passengers, would afford such carriers an opportunity to earn that operating income equiva-

lent to the rate of return established by the regulatory commission having jurisdiction in the carrier's last rate case (See committee report to accompany S. 1745, Calendar No. 857, 87th Congress, 1st Session, dated September 5, 1961). To any reasonable person, such action constitutes not only recognition, but acceptance by the Congress of this Commission's treatment of Transit on rate of return.

### CONCLUSION

In the determination of just and reasonable rates, it is the result reached and not the method employed which is controlling. The ultimate question is the totality of the consequences, and if the Commission's findings produce no arbitrary result, the Court's inquiry is at an end, F. P. C. v. Hope Natural Gas Company, 321 U. S. 591, 88 L. Ed. 333, 64 S. Ct. 281.

We need only look at the record to determine the consequences of the Commission's Order. The end result attained from the rate schedule authorized is that the vast majority of passengers in the District of Columbia have been able to utilize a token rate of 20¢ per ride<sup>11</sup> as compared with a 20¢ cash fare and a 19¢ token fare (5 for 95¢) as of the time that Transit began operation in August, 1956. The Commission has successfully maintained this level of fares for the majority of passengers in spite

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<sup>11/</sup> Expert testimony adduced at hearing indicated a range from 70 to 90% of Transit's passengers would enjoy the 20¢ rate. With the benefit of hindsight we know the actual figure to be about 75%.

of the inflationary trend, local and national; added expenses of Transit amounting to hundreds of thousands of dollars brought about by increased wages and benefits under union contract (TR 101); increased costs incident to improvement of existing facilities and the build-up in Washington of the largest and most modern fleet of air-conditioned buses in the world (TR 46). All of this has been accomplished within the framework of the unusual Congressional Franchise granted to assure the Washington Metropolitan Area of an adequate transportation system operating as a private enterprise. Neither Transit nor the public can reasonably complain of results such as these, and as previously indicated the Commission's regulation of Transit under the Franchise has been given tacit, if not express approval by the Congress as of date no later than September, 1961.

The decision of the District Court dismissing appellants' complaint and affirming Order No 4631 should be affirmed.

Respectfully submitted,

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## APPENDIX 1a

Prior to the sale of Capital Transit to D. C. Transit System, Inc., the Congress was considering a bill proposing to restore a franchise to the predecessor company that would establish a system rate base as of July 31, 1955, of about \$20,000,000. In reporting the bill to the House, Congressman Harris stated:

"In spite of these actions the Commission in 1954 contended that the depreciation reserve was deficient in the amount of \$2.4 million owing to alleged obsolescence of street railway properties. It is needless for me here to go into this record, or the fact that despite this contention the Commission agreed it might be rectified by a reduction in capital which had the effect that dividends might be paid out of capital surplus, a procedure which the Securities and Exchange Commission felt would be not in keeping with accepted accounting practice. Suffice it, that in adopting the rate base figure set out in this bill, the committee has accepted the adequacy of the depreciation reserve as stated on the books of the company. To make this clear, the bill also incorporates into the franchise the 1953 depreciation rates on various classes of property in effect as of July 31, 1955, for the future depreciation of the depreciable property in the property account as of that date.

..This is not to say that the committee is of the opinion that property no longer employed in the performance of the transportation service cannot be taken out of the property account, the undepreciated value and abandonment loss capitalized, and written off over future years at different but accepted rates. To do other would gainsay the provisions of the bill relating to a plan of conversion from street railway to all-bus operations.



## APPENDIX 1b

But it is to say that, regardless of what might be the committee's opinion with respect to the elements constituting the proper evaluation of a rate base, the Public Utilities Commission, having adopted and followed the original cost-less-depreciation method for these years, and predicated the allowed rate of return upon such method, should be consistent in its application of this method.

In addition to the allowance of \$20,256,000 representing the net investment in property, plant and equipment as of July 31, 1955, the rate base also includes a sum of \$1 million for cash working capital and a reasonable amount for material and supplies. In passing, it may be noted that the \$20 million figure for net property account as of last July, has been reduced through the operation of the depreciation account to \$18,832,556 as of March 31, 1956. Accordingly, as of this time, the total rate base approximates about \$20 million."

\* \* \*

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\* 102 Congressional Record 8292, May 16, 1956.

## APPENDIX 2

In spite of the fact that the Congress had considered establishing a rate base of \$20,000,000 for the predecessor company (Appendix 1), it did not do so for Transit. Congressman Harris reported in the following vein to the House following the House-Senate conferences on S. 3070, which became the Franchise.

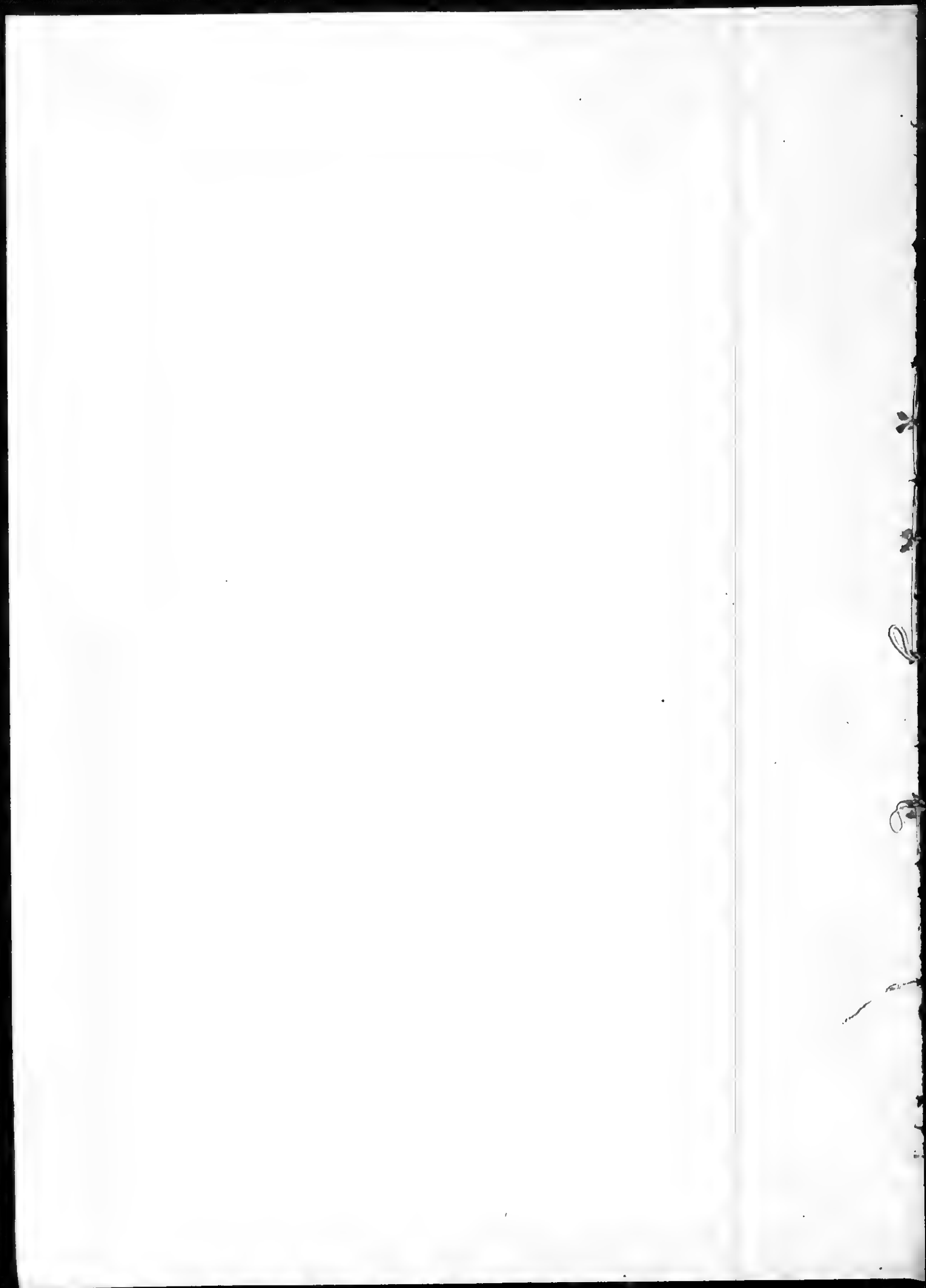
\*\*\*\*The same general tax concessions based upon a 6 1/2 per cent return, handling of rate matters and maintenance for a year of present fares, snow removal, and so on, as were in the House bill, are in the franchise here proposed.

Inasmuch, however, as the new group is definitely committed to a conversion of street railway to all-bus operations within a 7-year period, and is also acquiring the existing properties at a figure substantially below the amount at which they are carried on the books of Capital Transit, there is no specific provision in this franchise setting the rate base. In this connection, also, provision is made permitting the Public Utilities Commission, if conditions warrant, to calculate the rate of return under an operation-ratio method rather than the rate-base method hitherto employed."

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\* 102 Congressional Record 13580, July 19, 1956.



WILBUR K. MILLER

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BRIEF FOR APPELLEE  
D. C. TRANSIT SYSTEM, INC.

UNITED STATES COURT OF APPEALS  
FOR THE DISTRICT OF COLUMBIA CIRCUIT *United States Court of Appeals  
For the  
District of Columbia*

FILED NOV 29 1961

No. 16,454

*Joseph W. Stewart*  
CLERK

LEONARD N. BEBCHICK, AND  
LEONARD S. GOODMAN

APPELLANTS

VS.

PUBLIC UTILITIES COMMISSION OF  
THE DISTRICT OF COLUMBIA, AND  
D. C. TRANSIT SYSTEM, INC.

APPELLEES

APPEAL FROM AN ORDER OF THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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### QUESTIONS PRESENTED

1. Did the United States District Court commit reversible error in holding that the findings of the Public Utilities Commission in Order No. 4631 are supported by the record, and are neither unreasonable, arbitrary nor capricious.

2. In any event, are the questions raised by Appellants rendered moot as a result of Order No. 4735 of the Public Utilities Commission of the District of Columbia dated January 18, 1961, which order was subsequent to and superseded the order herein complained of, Order No. 4631, dated March 2, 1960.

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

---

No. 16,454

---

Leonard N. Bebchick, and  
Leonard S. Goodman

Appellants

vs.

Public Utilities Commission of  
the District of Columbia, and  
D. C. Transit System, Inc.

Appellees

APPEAL FROM AN ORDER OF THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT OF COLUMBIA



## SUBJECT INDEX

COUNTER-STATEMENT OF THE CASE .....	1
SUMMARY OF ARGUMENT .....	3
ARGUMENT .....	5
I.    THE ORDER OF THE COMMISSION WAS REASONABLE AND MAY NOT BE RE- VERSED BY THIS COURT .....	5
A.    THE SCOPE OF REVIEW HEREIN IS LIMITED TO A DETERMINATION OF WHETHER OR NOT THE ORDER OF THE COMMISSION WAS REASONABLE IN THE LIGHT OF THE RECORD.....	5
B.    THE ORDER OF THE COMMISSION WAS AMPLIFY SUPPORTED BY ITS FINDINGS, CONCLUSIONS, OPINION AND THE RECORD HEREIN .....	7
C.    APPELLANTS' ARGUMENTS AS TO TRANSIT'S SYSTEM RATE BASE ARE WITHOUT MERIT.....	15
D.    THE COMMISSION'S ALLOWANCE FOR TRACK REMOVAL AND REPAVING EXPENSES WAS PROPER .....	24
E.    THE COMMISSION'S ALLOWANCE FOR DEPRECIATION WAS PROPER .....	31
(1) Rail properties .....	31
(2) Bus properties .....	35
F.    APPELLANTS' ALLEGATIONS OF OTHER ERRORS ARE TOTALLY WITHOUT MERIT .....	37
II.    THE QUESTIONS RAISED BY APPELLANTS HAVE BEEN RENDERED MOOT AS A RESULT OF COMMISSION ORDER NO. 4735, DATED JANUARY 18, 1961 .....	39

III. CONCLUSION.....	48
----------------------	----

APPENDIX

# CASES CITED

<u>Atlantic Coast Line R.R. Co. v.</u> <u>Florida, 295 U.S. 301 (1934)</u> .....	44
<u>American Overseas Airlines v. Civil</u> <u>Aeronautics Board, 254 F. 2d</u> <u>744 (D.C. Cir., 1958)</u> .....	30
<u>American Power &amp; Light Co. v.</u> <u>Securities and Exchange Commission,</u> <u>329 U.S. 90 (1946)</u> .....	36, 37
<u>Board of Public Utility Commissioners</u> <u>v. Componia General De Tabacos</u> <u>De Filipinas, 249 U.S. 425 (1918)</u> .....	43
<u>Colorado Interstate Gas Co. v.</u> <u>Federal Power Commission,</u> <u>324 U.S. 581 (1945)</u> .....	32, 33
<u>Federal Power Commission v.</u> <u>Hope Natural Gas Co.,</u> <u>320 U.S. 591 (1944)</u> .....	6, 7
<u>Federal Power Commission v.</u> <u>Interstate Natural Gas Co.,</u> <u>336 U.S. 577 (1948)</u> .....	47
<u>Fleming v. Knudson &amp; Mercer Lumber Co.,</u> <u>159 F. 2d 212 (7th Cir., 1947)</u> .....	43
<u>Fleming v. Munsingwear, Inc.,</u> <u>162 F. 2d 125 (8th Cir., 1947)</u> .....	43
<u>In the Matter of D. C. Transit System, Inc.,</u> <u>38 P.U.R. 3d 19 (1961)</u> .....	16, 39
<u>In the Matter of Application of</u> <u>D. C. Transit System, Inc.,</u> <u>P.U.C. No. 3602, Order No. 4480</u> <u>of August 28, 1959</u> .....	18
<u>Keco Industries, Inc. v. Cincinnati</u> <u>&amp; Suburban Bell Telephone Co.,</u> <u>166 Ohio 254, 18 P.U.R. 3d 108</u> <u>(1957) App. dism'd., cert. denied</u> <u>355 U.S. 182</u> .....	46

<u>Mandel Bros., Inc. v. Chicago Tunnel</u> <u>Terminal Co., 2 Ill. 2d 205, 117</u> <u>NE 2d 774 (1954) .....</u>	44, 45
<u>Pennsylvania Water &amp; Power Co. v.</u> <u>Federal Power Commission,</u> <u>193 F. 2d 230 (D.C. Cir., 1951),</u> <u>aff'd 343 U.S. 414 (1952) .....</u>	47
<u>Public Utilities Commission v.</u> <u>Federal Power Commission,</u> <u>205 F. 2d 116 (3d Cir., 1953) .....</u>	33
<u>Spiegel v. Public Utilities Commission,</u> <u>226 F. 2d 29 (D.C. Cir., 1955)</u> <u>cert. denied, 350 U.S. 904 (1955).....</u>	17
<u>Spiegel v. Public Utilities Commission,</u> <u>247 F. 2d 84 (D.C. Cir., 1957).....</u>	17
<u>United Gas Pipe Line Co. v. Mobile</u> <u>Gas Service Corp., 350 U.S. 332 (1956).....</u>	47
<u>United States v. Pierce Auto Freight</u> <u>Lines, 327 U.S. 515 (1945).....</u>	33
<u>Washington Gas Light Co. v. Baker,</u> <u>188 F. 2d 11 (D.C. Cir., 1950),</u> <u>cert. denied, 340 U.S. 952 (1951).....</u>	32, 46
<u>Washington Gas Light Co. v. Baker,</u> <u>195 F. 2d 29 (D.C. Cir., 1951) .....</u>	39
<u>Washington, Marlboro &amp; A.M. Lines</u> <u>v. Public Utilities Commission,</u> <u>114 F. Supp. 328 (1952), aff'd.,</u> <u>206 F. 2d 490 (D.C. Cir., 1953).....</u>	6

### STATUTES CITED

Title 43, Section 315 of the District of Columbia Code, 1951 Ed. ....	35, 36
Title 43, Section 401 of the District of Columbia Code, 1951 Ed. ....	45
Title 43, Section 408 of the District of Columbia Code, 1951 Ed. ....	45
Title 43, Section 703 of the District of Columbia Code, 1951 Ed. ....	42
Title 43, Section 706 of the District of Columbia Code, 1951 Ed. ....	5, 6
Title 43, Section 707 of the District of Columbia Code, 1951 Ed. ....	42, 45
Title 43, Section 902 of the District of Columbia Code, 1951 Ed. ....	44
Title 43, Section 906 of the District of Columbia Code, 1951 Ed. ....	45
Joint Resolution of Congress, Act of September 15, 1960, 74 Stat. 1031.....	48
Act of July 24, 1956, 70 Stat. 598 (the "Franchise").....	8, 10, 14, 24, 27, 29, 30, 31, 42

### MISCELLANEOUS

Welch, Preparation for the Utility Rate Case, pp. 166-167, 282 (1954).....	13, 17
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### COUNTER-STATEMENT OF THE CASE

Appellants' statement of the case is not a complete description of the events which have transpired in this proceeding. It does not address itself to the fare proposal originally submitted by D. C. Transit System, Inc. ("Transit") and to other matters which may be helpful to the Court. Transit therefore deems it appropriate to make this counter-statement of the case to supplement Appellants' statement.

On November 6, 1959 Transit filed with the Public Utilities Commission of the District of Columbia ("Commission") a Petition for a change in its schedule of rates to be charged in the District of Columbia. By its Order No. 4585, dated November 9, 1959, the Commission suspended the proposed schedule of rates for a period of 120 days and ordered an investigation and public hearing relative to Transit's Petition.

The rate schedule in effect on November 6, 1959 was as follows:

Cash fare	-	20¢
Token fare	-	20¢ (in units of 5 for \$1.00)
School fare	-	10¢ (in units of 10 for \$1.00)

In place of such rate schedule Transit's Petition



proposed the following:

(A) Schedule of Rates Effective November 16, 1959

	<u>Adult</u>	<u>School Fare</u>
Cash Fare Other Than Rush Hours	20¢	10¢
Cash Fare During Rush Hours	25¢	10¢

(B) Schedule of Rates Effective November 1, 1960

	<u>Adult</u>	<u>School Fare</u>
Cash Fare	25¢	10¢

Hearings on the proposed rate schedule commenced on November 24, 1959 and were continued through 11 sessions until their conclusion on February 19, 1960. A total of 96 exhibits were offered in evidence and 2,077 pages of testimony were taken. Three witnesses testified on behalf of Transit, two witnesses testified on behalf of the Commission, and five witnesses testified on behalf of intervening citizens' associations and/or individual intervenors. In addition, a number of representatives of the public appeared and made statements on the record presenting their views as to the proposed rate schedule.

Following the completion of the testimony and oral argument, the Commission, on March 2, 1960, issued its Order No. 4631, (Joint Appendix, page 1, hereinafter cited merely as "J. A. \_\_\_\_\_"), which ordered the following rate schedule

into effect on March 6, 1960:

Cash fare	-	25¢
Token fare	-	20¢ (in units of 5 for \$1.00)
School fare	-	10¢ (in units of 10 for \$1.00)

The rate schedule adopted ("Commission Rate Schedule") was proposed by the staff of the Commission (J. A. 2-3) and the sole difference between it and the rate schedule previously in force was an increase of 5¢ in the cash fare.

In all other respects Appellants' "Statement of the Case" is accurate and need not be expanded upon herein.

#### SUMMARY OF ARGUMENT

The scope of review herein is limited to a determination of whether or not the order and findings of the Commission were reasonable in light of the record.

There is more than ample support in the record for the essential findings and conclusions of the Commission.

The Commission's determination to use the gross operating revenue ("GOR") method for rate making purposes in this proceeding, is more than amply supported by the provisions of Transit's Franchise and by Transit's conversion to bus operations pursuant to the terms thereof.

The Commission's findings that Transit's net

operating income would be \$1,143,249 which, in turn, would be 4.1% on the GOR method, for the 12 month test period ending December 31, 1960, is more than amply supported by the testimony and exhibits of the witnesses.

The Commission's finding that a rate of return of 4.1% on the GOR method for Transit herein would be reasonable, is more than amply supported by Transit's Franchise; by the Commission's using the system-rate-base rate of return (7.14%) to test the reasonableness of the 4.1% return on the GOR method; by a determination of whether this rate of return afforded the company an opportunity to meet its interest expenses, pay reasonable dividends, retain earnings for contingencies and attract necessary capital; and by a comparison of this schedule of fares and the resulting rate of return with those in other comparable jurisdictions using the GOR method.

Appellants' arguments addressed to the system rate base findings of the Commission are largely irrelevant since the Commission clearly indicated that it had used the GOR method and not the system rate base method in determining the rate schedule herein. Moreover, Appellants' arguments are, as a matter of substance, erroneous and without merit.

Appellants' arguments addressed to the accrual for track removal and repaving expenses and for the allowance for depreciation allowed Transit by the Commission in determining the net operating income of Transit for the test period are without merit.

Appellants' allegations of "other errors" in this proceeding lack substance. The record herein fails to show that matters such as the corporate reorganization of Transit's parent company (D. C. Transit System, Inc., a Delaware corporation), the sale of stock by its grandparent company (Transportation Corporation of America), and Transit's banking policies, have any relevance whatsoever to the subject matter of this case. Moreover, appellants' contentions in these regards rest upon unsupported suspicion and surmise.

The questions raised by appellants have been rendered moot as a result of Commission Order No. 4735 which supersedes the Order herein.

#### ARGUMENT

##### I

#### THE ORDER OF THE COMMISSION WAS REASONABLE AND MAY NOT BE REVERSED BY THIS COURT

- A. The Scope of Review Herein is Limited to a Determination of Whether or Not the Order of the Commission was Reasonable in the Light of the Record.

The Court's power to review the Order of the Commission is governed by Title 43, Section 706 of the District of Columbia Code, 1951 Ed. which provides:

"In the determination of any appeal from an order or decision of the Commission the review by the court shall be limited to questions of law, including constitutional

questions; and the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary or capricious."

Pursuant to this statute, the Court must sustain the determination of the Commission unless it appears that the Commission acted unreasonably, arbitrarily or capriciously.

This Court may not, of course, substitute its judgment for that of the Commission or otherwise decide this case de novo. Review is limited to the question of whether the Commission, as a matter of law, acted improperly. There is a strong presumption of validity attaching to the Commission's Order and those who would upset such Order bear the heavy burden of showing that it was improper as a matter of law.

When supported by some evidence, the Commission's determination will not be set aside even though the Court might conceivably have reached a different conclusion had this matter been before it de novo. See, e.g., Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944); Washington, Marlboro & A.M. Lines v. Public Utilities Commission, 114 F.Supp. 328 (1952), aff'd, 206 F.2d 490 (D. C. Cir., 1953).

In the Hope case, the Supreme Court enunciated

the following fundamental principles of utility regulation (p. 602):

"It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry \*\*\* is at an end. The fact that the method employed to reach that result may contain infirmities is not then important. Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a presumption of validity."

The foregoing statements as to the scope of review herein are so elementary that there can be no dispute about them. These principles would hardly require restatement were it not for the fact that the main thrust of Appellants' brief is nothing more than a plea for this Court to substitute its judgment for that of the Commission.

B. The Order of the Commission was Amply Supported by its Findings, its Conclusions, its Opinion and the Record Herein.

The Commission, after extensive hearings (eleven sessions, 96 exhibits and 2,077 pages of testimony) ordered an increase in Transit's cash fare from 20¢ to 25¢. In support of this order, the essential findings and conclusions of the Commission were:

(1) The GOR method should be used for determining the schedule of rates for Transit herein (J. A. 1);



(2) The Commission's rate schedule would produce for the test period net operating income of \$1,143,249, or a rate of return of 4.1% on the GOR method (J. A. 2); and

(3) The rate of return of 4.1% on GOR method for Transit herein was fair and reasonable (J. A. 2-3).

There is more than ample support in the record for these essential findings and conclusions.

In support of its adoption of the GOR method, the Commission relied on Section 4 of Transit's Franchise, (70 Stat. 598 [1956], hereinafter cited merely as "Franchise") which declares that:

"the Congress finds that the opportunity to earn a return of at least 6 1/2 per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on either the system rate base or on gross operating revenues would not be unreasonable, and that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible and as conditions warrant; and if conditions warrant not later than August 15, 1958." (Emphasis supplied)

The Commission properly viewed Section 4 as a legislative mandate to apply the GOR method as promptly as conditions warranted (J. A. 1, 6-8, 43-45). The Commission considered the history and background of the Franchise Act and determined that the applicable conditions justifying a

change to the GOR method from the rate base method it had theretofore used were (1) a conversion of street railways to bus operations by Transit measured by an abandonment of 55% of street railway track; (2) completion of 51% of conversion to bus operations; and (3) the adoption by Transit of a program for replacing buses sixteen or more years old (J. A. 7, 43-45). Since the record demonstrates beyond peradventure that Transit had complied with the foregoing conditions (J. A. 9, 46, 47, 54, 97-109)\*, the Commission was justified in adopting -- if, indeed, it was not required to adopt -- the GOR method in this proceeding.

The second essential finding and conclusion was that the Commission Rate Schedule would result in net operating income of \$1,143,249 during the test period, and that such income would represent a rate of return of 4.1% on the GOR method (J. A. 2-3). Elaborate detailed breakdowns in support of the conclusion are contained in Exhibits 36 and 40 at pp. 33-34 of the Appendix to this Brief and at J. A. 51-54, and amply sustain the Commission's determination as to the net

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\* Appellants do not challenge Transit's compliance with the conditions established by the Commission for the adoption of the GOR method.

operating income\* which would result from the Commission Rate Schedule.

The final essential finding and conclusion of the Commission was that a rate of return of 4.1% on the GOR method was reasonable (J. A. 3). This finding and conclusion also is more than amply supported by the record. Thus, Section 4 of Transit's Franchise specifically states that:

"Congress finds that the opportunity to earn a rate of return of at least 6 1/2 per centum net after all taxes \*\*\* would not be unreasonable" (Emphasis Supplied)

At the very least, this represents a determination by Congress that a rate of return of 6.5% - and, a fortiori, a rate of return of 4.1% - is, as a matter of law, reasonable. If the Commission had nothing else before it but Transit's Franchise, it would thus have had ample support in the provisions of Section 4 for its conclusion that the rate of return here under attack was a reasonable one. In point of fact, however, the record contains substantial additional evidence demonstrating the reasonableness of the 4.1% rate of return.

The Commission tested the reasonableness of the 4.1% rate of return by computing Transit's return on the

\* Appellants argue that the Commission allowed Transit "arbitrary and unreasonable operating expenses" resulting in an understatement of Transit's net operating revenues. (Appellants' Brief, p. 18). This contention of Appellants is dealt with at pp. 24-37 hereof.

system rate base method under the proposed rate schedule (J. A. 2, 19-25). After extensive investigation of Transit's system rate base, the Commission concluded that the new fare structure would result in a return of 7.14% on the system rate base method (J. A. 3). This 7.14% rate of return on the system rate base method served to confirm the Commission's determination that the 4.1% return on the GOR method was reasonable.

As still another means of determining the reasonableness of the 4.1% rate of return on the GOR method, the Commission considered whether net operating income in the amount of \$1,143,249 would allow Transit sufficient income to pay interest, declare reasonable dividends, retain sufficient earnings for contingencies and attract capital (J. A. 27). Interest charges were found to be \$317,000 (J. A. 24, 133). It was concluded that dividends of \$500,000 per annum on its capital stock were reasonable, and that the retention of approximately \$327,000 in earnings would also be reasonable (J. A. 24, 25). It was the position of the Commission's staff witness that approximately \$800,000 after interest payments would be available for a return of equity

capital under the proposed rates, and that such amount was a proper one for the transit industry (J. A. 134).

Mr. Edward A. Roberts, an independent transportation consultant retained by the Commission, testified that the fare schedule adopted would provide a fair and reasonable return for the company in this case (J. A. 132-133). Mr. William Falk, a member of the Commission's staff, testified that the resulting return on equity capital for Transit under the circumstances of this case would be reasonable (J. A. 145-147). Mr. Falk further testified that the declining characteristic of the transit industry and its inability to absorb unanticipated future costs, must be considered in fixing earnings for Transit (Appendix to this Brief, 22-23).

In addition, the record contains much testimony stressing Transit's need for additional revenue to maintain its ability to attract capital (Appendix to this Brief, 17); to enable it to meet its new equipment purchase obligations (Appendix to this Brief, 17); to enable it to proceed with the construction of an essential and vastly expensive new maintenance base (Appendix to this Brief, 17); to meet greatly increased labor costs; to meet the increased replacement cost of equipment due to inflation; and to meet the financial demands imposed by the company's conversion program (Appendix to this Brief, 16-23). These matters were covered exhaustively

throughout an extensive record. They are pointed out here merely to demonstrate the extent of the subject matter considered by the Commission in reaching its result as to the reasonableness of Transit's rates.

Finally, as a fourth check on the reasonableness of the 4.1% rate of return on the GOR method, the Commission noted that:

"The record shows that many regulatory commissions have utilized the operating ratio method with varying results. For example, a study by the American Transit Association of 80 decisions shows a wide range of operating ratios from a maximum of 99.8% to a minimum of 87.4%, after taxes." (J. A. 24)

In this connection it is significant to note that Welch, "Preparation for the Utility Rate Case", p. 282 (1954) states that operating ratios allowed by state public utility commissions using the GOR method ranged from 87.40% to 96.08% after taxes, and hence that the corresponding rates of return ranged from 12.60% to 3.92%. The operating ratio of 95.9% allowed to Transit in this proceeding (i.e. the reciprocal of Transit's 4.1% rate of return herein) is thus somewhat on the low side and is far from unreasonable, arbitrary or capricious.

The reasonableness of the 4.1% rate of return allowed Transit is further confirmed by the fact that the 25¢ adult cash fare is itself reasonable in terms of fares charged in other cities. No less than 11 of the 29 largest cities in this country (exclusive of the District of Columbia)



charge a 25¢ fare. Moreover, the 20¢ token fare of Transit is exceeded or equalled by 16 of such cities. (J. A. 50)

In summary, it is clear that the essential findings of the Commission are more than amply supported by the record. In fact, the crucial determination of the Commission - that the rate of return of 4.1% on the GOR method is reasonable - can be sustained on no less than four independent grounds.

1. Congress in Transit's Franchise determined, as a matter of law, that a rate of return of 6.5% was reasonable and that, a fortiori, a rate of return of 4.1% was proper.

2. The net operating income resulting from the Commission Rate Schedule for the test period (\$1,143,249) would produce a rate of return of 4.1% on the GOR method, the reasonableness of which is corroborated by the fact that such income would represent a system rate base rate of return of 7.14%.

3. The rate of return permitted would allow Transit sufficient net operating income to cover interest charges, pay reasonable dividends, retain sufficient earnings for contingencies and the replacement of equipment at higher price levels and to attract needed capital investment.

4. Such rate of return and the Commission Rate Schedule itself are conservative when compared with those in other jurisdictions.

C. Appellants' Arguments as to Transit's System Rate Base are Without Merit.

The bulk of Appellants' Brief is devoted to an attack on Transit's system rate base as determined by the Commission (Appellants' Brief, pp. 37-60). Before turning in detail to Appellants' arguments on this point, we would remind the Court that the Commission did not use the system rate base method in determining the schedule of rates herein. At most, the system rate base was used as a means of confirming or testing the reasonableness of the rates determined by the GOR method. Appellants' argument to the contrary is totally invalid and without merit (Appellants' Brief, pp. 60-68).

It could hardly be clearer that, in its Order herein, the Commission relied exclusively and entirely on the GOR method. Thus, the Commission, as its initial finding, held:

"That the Company has complied substantially with the intent of the Franchise Act and with the conditions heretofore indicated by the Commission as warranting the utilization of the gross operating revenue method for rate-making purposes in keeping with the legislative policy declared in Section 4 of the Act."  
(J. A. 1)

Based on this finding, the Commission concluded:

"That the gross operating revenue method should be utilized to fix rates in this proceeding." (J. A. 2)

The Commission devoted no less than six pages of its opinion to the reasons why it was utilizing the GOR method (J. A. 5-11), stating clearly and unequivocally that "the gross operating revenue method should be utilized to fix rates in this proceeding" (J. A. 10-11) and that the "rate base-rate of return method should be employed \*\*\* to test the reasonableness of the rate of return computed under the gross operating revenue method" (J. A. 11).

Moreover, in the subsequent rate case, the Commission specifically stated that it had used the GOR method in determining rates in the instant proceeding. P.U.C. No. 3640, In the Matter of D. C. Transit System, Inc., 38 P.U.R. 3d 19 (1961).

In view of the foregoing, Appellants' contention that the GOR method was not used is absurd.

Since the Commission used the system rate base method merely as one of four methods of confirming the reasonableness of the rates which it had fixed by the GOR method, it is plain that, even if there were substantial merit to the Appellants' attack on the rate base determinations of the Commission, Appellants' arguments would hardly constitute grounds for reversal since the rates determined are reasonable without regard to any system rate base analysis.

The Commission found Transit's rate base to be \$16,016,819 (J. A. 2). The development of this rate base

from the exhaustive testimony and numerous exhibits is found in the Commission's opinion at J. A. 20. Briefly, the Commission arrived at this figure by using the original cost (plus additions, less depreciation) of Transit's predecessor, Capital Transit Company ("Capital"), and averaging such figure with Transit's net investment in rate base property (plus additions, less depreciation) based on the purchase price paid for the assets of Capital.

Appellants contend that, as a matter of law, the rate base found by the Commission was improper since it exceeds the capital investment of Transit in the assets of Capital (Appellants' Brief, pp. 39-45). Appellants fail to cite a single case which so holds. In point of fact, this Court held in Spiegel v. Public Utilities Commission, 226 F.2d 29 (D. C. Cir., 1955), cert. den. 350 U.S. 904 (1955) and 247 F.2d 84 (D. C. Cir., 1957) that the Commission could properly use a rate base resting on original cost under circumstances such as are here present. Welch, "Preparing for the Utility Rate Case" (1954), pp. 166-167 confirms that it is by no means uncommon to allow a rate of return on original cost even though the property was acquired at below book value in an arm's-length transaction. There is, therefore, no merit in the contention that Transit's rate base is, as a matter of law, limited to Transit's investment in the assets of Capital.

Moreover, Appellants' contention that the Commission "arbitrarily departed" (Appellants' Brief, p. 41) from its previous practice when it used original cost in this proceeding is equally without merit. The Commission has in the past used the original cost method even though the assets were no longer owned by the company which originally placed them in use. For example, in its Order No. 4480 of August 28, 1959, P.U.C. No. 3602, In the Matter of Application of D. C. Transit System, Inc., the Commission gave equal weight to purchase price and original cost, precisely as it has here done, to determine rate base. The testimony of witness Falk at J. A. 141 and P.U.C. No. 3592 at J. A. 85 indicate other instances when this averaging technique has been employed by the Commission.

Appellants argue further that the Commission's rate base is erroneous because it includes the amount of the

acquisition adjustment account.\* Presumably what they mean is that to the extent the acquisition adjustment account is included in the historical cost, the historical cost should not have been used at all. This argument we have answered at length above and need not be answered separately again.

The Commission persuasively and in great detail sets forth the reasons why it here chose to determine rate base by averaging historical cost with acquisition cost (J. A. 21-23), and it can hardly be said that the Commission's action was unreasonable or arbitrary.

Appellants' insistence upon the exclusive use of a purchase price rate base stems largely from the testimony of their witness, Mr. Thomas G. Harris. The Commission's opinion (J. A. 15-18) indicates that the views expressed by this witness were given careful consideration, and at page 22 of the opinion (J. A. 20-21) the Commission notes in some detail the reasons why it felt unable to accept Mr. Harris' recommendation as to rate base. The Commission found that Mr. Harris'

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\* The assets acquired from Capital are carried on Transit's books at Capital's depreciated original cost. As an accounting device to limit Transit's depreciation to the cost of acquisition of Capital's assets, an acquisition adjustment account equal in amount to the difference between Capital's depreciated original cost and Transit's acquisition cost was established in the amount of \$10,339,041. This acquisition adjustment account is being written off annually in the amount of \$1,033,904. The result of the write off is that depreciation is annually reduced by the amount of \$1,033,904, with the net effect being that depreciation is allowed as if Transit carried Capital's assets at depreciated acquisition cost. This is fully detailed in the Commission's opinion (J. A. 12-13), and in Exhibit No. 2 (J. A. 87).



recommendations contained "inconsistencies" and were not in accord with the Commission findings as to the value of the rail properties owned by Transit.

At pages 55-56 of their Brief, Appellants argue that the rate base figure adopted by the Commission includes "in effect" certain operating reserves. They contend that the "end result" of the Commission's determination was "the inclusion in the rate base of such operating reserves as the 'Reserve for Track Removal and Repaving' or the 'Reserve for Injuries and Damages'". The record belies this assertion.

But, say the Appellants, because the reserves for track removal and repaving and for injuries and damages were not deducted from the gross investment figures, such reserves were, in effect, included in the rate base. The simple and direct answer to this contention is that neither of these reserves was or is a valuation reserve. Instead, each of them is a liability reserve, i.e., each of them was built up out of income as a reserve to cover the specific liability indicated by its name - not for the purpose of recovering investment. Therefore, it would be improper to treat either of such reserves as a recovery of investment and deduct it in determining rate base. Yet this is what Appellants contend should have been done.

Apparently, Appellants' view is based upon a belief

that reserves for track removal and repaving and for injuries and damages are the same kind of reserves as the reserves for depreciation. This view misses the crucial distinction that the depreciation reserve is entirely different from the other two reserves. A depreciation reserve is accrued for the purpose of recovering investment and, of course, must necessarily be deducted from original cost in determining rate base. The reserves for track removal and repaving and for injuries and damages are liability reserves accrued for the purpose of meeting liabilities. The depreciation reserve was properly deducted from the gross investment because it represents recovery thereof. The liability reserves were not deducted from the gross investment (and could not properly have been) because they do not represent any recovery thereof. This being true, the Appellants simply are wrong in their contention that failure to deduct the liability reserves was "in effect" to include them in the rate base determined by the Commission.

At page 58 of their Brief, Appellants contend that the Commission's system rate base unlawfully includes certain rail properties. Their point is that certain of these rail properties have been abandoned by Transit and may not be included in its rate base since Transit's investors have been

heretofore fully compensated for such property. Appellants' contention is based upon their witness Harris' theory that Transit purchased its properties at a price which had been discounted by the seller to cover fully the undepreciated values associated with street railway properties, so that, in effect, Transit recovered the cost of such properties at the very time it acquired them.

The Commission carefully considered witness Harris' opinion and rejected it for ample reasons. The Commission's statement would be difficult to improve upon, and was as follows (J. A. 16):

"The witness \*\*\* states that his proposals were not related to any consideration of the conditions of the agreement dated July 7, 1956, whereby D. C. Transit acquired all of the assets of Capital Transit Company. Based on our reading of the record, however, we can reach no other conclusion but that his proposals are based in large measure on his speculation of what considerations entered the minds of the contracting parties as of July 7, 1956. The record shows that as of the time of testifying, he had not read the agreement and was not familiar with the terms thereof.

"The record contains evidence to the effect that the purchase price paid by D. C. Transit of \$13,540,000 was based on a market price of \$14.00 per share for the 960,000 shares of Capital Transit Company common stock outstanding as of the date of the agreement, plus an additional amount of \$100,000 to meet an offer of another prospective purchaser. What other considerations

may have entered the minds of the contracting parties is not a matter of record. Mr. Harris has concluded, however, that the purchase price paid \*\*\* was based on writing off all rail facilities as being of no value and that the purchase price also reflected the liability of the Capital Transit Company for track removal and repaving, which he states were assumed by D. C. Transit.

"We fail to see how rail facilities could be considered as valueless when they had a remaining useful life of seven years and were at the time producing annual revenues of approximately \$12,000,000."

Thus, the sole underlying basis for Appellants' argument is shown to be contrary to the evidence. Certainly, it cannot be seriously argued that the Commission's rejection of Mr. Harris' theory was arbitrary, capricious or unreasonable.

Since Transit has not recovered the undepreciated cost of the rail properties, either in the manner which Appellants suggest or in any other manner, there was no error in the Commission's inclusion of rail properties in its rate base determination.

It is therefore clear that Appellants' contentions as to the "errors" made by the Commission in determining Transit's rate base are wholly and entirely without substance. Moreover, even assuming, arguendo, that the Commission did err in computing Transit's rate base, the system rate base method was used merely as a means of corroborating the reasonableness of the rates determined by the GOR method,

and an error in Transit's system rate base in these circumstances hardly is a ground for reversing the determination of the Commission.

D. The Commission's Allowance for Track Removal and Repaving Expenses Was Proper.

Appellants argue that in determining Transit's net operating income the Commission erred in allowing Transit \$1,044,196 as an accrual deduction for track removal and repaving expense.

Under Section 7 of its Franchise (Appellants' Brief, Appendix A), Transit is obligated to remove its street railway tracks and to repave the streets upon such terms and conditions as the Commission prescribes. Based on Commission staff studies and engineering estimates, as well as a consideration of the company studies, the Commission concluded that the total cost of this program would be approximately \$10,441,958 (J. A. 13). In accordance with standard utility accounting practices, the Commission thereupon directed that such cost be provided for by annual accruals against revenues over a ten year period, at the rate of \$1,044,196 per year (J. A. 13).

Appellants' contentions with respect to this accrual are that the Commission's allowance of \$1,044,196 was excessive and that, in any event, this item is not properly an expense item to be charged against operating revenues, but is instead a capital item; a burden assumed by Transit's investors when

they acquired the business in exchange for a reduced purchase price for Capital's assets (Appellants' Brief, pp. 18-23).

It is Appellants' opinion that the accrual of the cost of track removal was excessive since the amount accrued exceeds Transit's expenditures to date for that purpose. In so arguing, Appellants reveal a complete lack of understanding of the background and objectives of the annual accrual. The purpose served in permitting equal annual accruals over the ten year period was to spread the impact of this extraordinary expense over such period. It is self-evident that an attempt to provide for the expense on a current basis as desired by Appellants would be grossly unfair to both the company and the public, since it would cause violent fluctuations in Transit's income and expenses, which would, in turn, have to be reflected in the company's rates.

In the last analysis, accruing this item redounds to the benefit of the public since the company can operate with greater financial stability. The alternative would be to burden Transit's riders with enormous expenditures in the latter years of the track removal program. The rejection of this alternative by the Commission is obviously sound. Accordingly, the fact that during any portion of the period the company has expended more or less than the accrued amount is irrelevant.



Appellants also take exception to the aggregate amount allowed for track removal purposes, \$10,441,958. As we have already indicated the determination of this amount was based on the studies and estimates of the best available experts. Moreover, the Commission noted that the total amount expended might exceed or be less than this estimate, and that it was keeping the matter under continuous study so that, as future conditions dictated, adjustments might be made (J. A. 13). This position of the Commission finds substantial support in the record since witness Falk testified that not enough experience had been gained to warrant any change in the amount being accrued for track removal purposes (Appendix to this Brief, p. 21) and Appellants' witness Harris agreed that present experience was minimal (Appendix to this Brief, p. 25).

Appellants also urge that this item is not properly an operating expense at all, but is rather a capital item comprehended in the purchase price paid to Capital. In support of their position, Appellants place primary reliance upon the testimony of their witness, Mr. Harris (J. A. 218-221). They also purport to find similar support in positions taken by Transit in prior proceedings before the Commission (J. A. 83-84), in the testimony of Transit witnesses in prior proceedings (J. A. 68), and in the testimony of Transit and

staff witnesses in this proceeding (J. A. 128-129). Their references to the record do not, however, relate the entire story.

In the first place, while there is little doubt that witness Harris testified in support of Appellants' theory, Appellants overlook the fact that although the testimony of this witness was most ineffective and non-persuasive, it was nevertheless thoroughly considered by the Commission, and, for ample reasons, rejected (J. A. 15-21).

Secondly, Appellants' reliance upon Transit's position in the 1957 proceeding to which they refer (J. A. 83-84) is mistaken and misleading. That was a proceeding under Section 9(c) of the Franchise having to do with the company's conditional exemption from gasoline taxes. Nowhere therein did Transit agree that the track removal and repaving obligation had been comprehended by the purchase price paid for the business. In that proceeding, the Commission was confronted with the problem of devising a method of accounting for the excess of the net original cost of the properties as recorded by the previous owner over the price paid for the business by Transit, a figure of approximately \$10.3 million. In that proceeding, Transit made one accounting proposal and the staff made a separate proposal. The Commission adopted the proposal of its staff that Transit be allowed depreciation

on an original cost basis; that this depreciation be reduced by amortization of the \$10.3 million "excess" and that Transit be entitled to accrue the amount of the \$10,441,961 over 10 years for track removal and repaving costs. Against the reserve so accrued, actual expenditures were to be charged as and when made. This is explained in detail in the Appendix to this Brief at pp. 18-21 and at J. A. 83-84. An objective reading of the Commission's full report in that proceeding (J. A. 80-86) makes it clear that Appellants' reference does not support their argument here.

Thirdly, Appellants' reference to certain 1958 testimony of Transit's witness Flanagan (J. A. 68) is incomplete. While they contend that Mr. Flanagan's remarks constituted an admission that the track removal and repaving obligation had been assumed by Transit's investors, they fail to note that their own witness, Mr. Harris, on cross examination, admitted that Appellants' conclusion is the result of his "interpretation" of Flanagan's language, and that, in effect, the testimony referred to constituted no such admission (J. A. 228-229). Similarly, the Appellants conveniently ignore the fact that in this proceeding witness Flanagan explained his 1958 remarks, and testified specifically that the purchase price paid by Transit's investors had nothing

whatsoever to do with the obligation under the Franchise to remove tracks and repave streets (J. A. 240-241). Appellants also fail to note that in its opinion (J. A. 16-17), the Commission found in effect that since Mr. Flanagan's testimony in 1958 was offered in connection with proposals which differed materially from the position taken by the intervenors in this proceeding, such testimony was not relevant to this proceeding.

Finally, Appellants' reliance upon testimony of Transit's witness Flanagan and staff witness Falk in this proceeding (J. A. 128-129), as supporting their contention is simply contrary to the record. The testimony of Flanagan referred to was to the effect that Transit's Franchise imposes an obligation to remove tracks and repave streets. Mr. Flanagan made no reference to any relationship between the purchase price of the business and the track removal obligation.

So far as witness Falk is concerned, he merely indicated that he thought the track removal obligation was "an element" which may have been considered by the parties in arriving at the purchase price (Appendix to this Brief, p. 27). In other testimony, this witness specifically denied that the purchase price reflected any portion of an assumed liability for track removal (Appendix to this Brief, pp. 26-27). On

the contrary, this witness, and Transit's witness, both contended that the allowance for track removal and repaving which was approved by the Commission was a proper charge against revenues (Exhibits 10-A and 39, J. A. 51, Appendix to this Brief, 18, 20-21). There is no justification for Appellants' contention that either witness Falk or witness Flanagan supported their thesis that the track removal obligation is a capital item, and not an operating expense to be properly charged against revenues.

In support of their argument that the track removal allowance is an improper deduction, Appellants rely on this Court's decision in American Overseas Airlines v. Civil Aeronautics Board, 254 F.2d 744 (D. C. Cir., 1958). This case, however, does not support their position. There, the Court, referring to the unforeseeable losses arising out of a strike, noted, by way of dictum, that it would be improper (p. 750):

"to cushion a company in advance against unforeseen events which are not ordinary or necessary in the sense that ordinary and necessary expenses are forecast in a prospective rate case."

With the Court's statement Transit is, of course, in full agreement. In the instant case, however, the Commission had before it Transit's Franchise containing an explicit direction that track removal and repaving be undertaken and completed. There is nothing contingent about this obligation. There is nothing

unforeseen about the expense involved. The sole problem was to make adequate provision for such expense, and this is precisely what the Commission did.

E. The Commission's Allowance for Depreciation Was Proper.

(1) Rail properties

Appellants have questioned the propriety of the Commission's allowance for depreciation, insofar as it relates to Transit's rail properties.

As we have heretofore stated, Section 7 of Transit's Franchise (J. A. 93-94) requires that the company completely convert its street railway operation to an all bus operation. The statute orders the abandonment of street railway properties.

The record in this proceeding shows that as of December 31, 1959, the net undepreciated cost of Transit's rail properties was \$5,121,644 (J. A. 14, 48, 52). It shows also that as of January 3, 1960, pursuant to the statute Transit had abandoned 49.4% of its rail facilities (J. A. 14). Transit proposed that the full amount of net undepreciated cost of rail properties be recovered by extraordinary depreciation charges over the remainder of the period allowed for conversion (J. A. 110-111). The Commission, however, rejected Transit's proposal and limited its allowance of extraordinary depreciation to that portion of the rail properties actually abandoned on January 3, 1960 (J. A. 14-15).



Appellants' contention is twofold. Relying upon this Court's decision in Washington Gas Light Co. v. Baker, 188 F.2d 11 (D. C. Cir., 1950), cert. den. 340 U.S. 952 (1951), they contend that the Commission "failed to make the type of finding which this Court has directed to be made as a condition precedent to permitting depreciation and a return on abandoned property" (Appellants' Brief, p. 25). Secondly, they contend that no allowance whatsoever for depreciation of rail properties was warranted in this case.

Addressing their first contention, Baker does not prescribe the form the Commission's findings must take. In Colorado Interstate Gas Co. v. Federal Power Commission, 324 U.S. 581, 595 (1945), the Supreme Court ruled that so long as the path which the regulatory body followed can be discerned, its findings are adequate. In Baker, this Court's essential requirement was that, to facilitate judicial review, this Commission make clear the evidentiary support for its decision. Transit submits that in this case the Commission has made its reasons for allowing the depreciation complained of abundantly clear.

At page 15 of its opinion, the Commission points out that the depreciation estimates of both the Transit and staff witnesses were based upon depreciation rates prescribed by the Commission effective July 1, 1953 (J. A. 14, 74). At

page 16 of its opinion, based upon the concurring testimony of two witnesses, the Commission clearly found that the net undepreciated cost of Transit's rail properties amounted to \$5,121,644 (J. A. 14). On the basis of substantial evidence, therefore, the Commission clearly found that the investment in these rail properties had not been recovered by depreciation accruals. Appellants contend, however, that to justify any allowance for this unrecovered investment, the Commission was required to find that the investors had not already been compensated for the risk that these properties would be rendered obsolete prior to the full recovery of their undepreciated cost. Obviously such a finding is implicit in the Commission's opinion.

Formal and precise findings are not required.

Public Utilities Commission v. Federal Power Commission, 205 F.2d 116 (3d Cir., 1953). The Commission is not required to annotate to each finding the evidence supporting it. United States v. Pierce Auto Freight Lines, 327 U.S. 515, 529 (1945). The path followed by the Commission on this branch of the case is readily discernible from its opinion. Colorado Interstate Gas Co. v. Federal Power Commission, supra.

Appellants' witness Harris took the position that at the time Transit's investors acquired the business, they assumed not only the risk of obsolescence of the company's rail properties, but also the obligation to remove tracks and

repave the streets (J. A. 218-221). He testified that, in his opinion, this was demonstrated by (1) the fact that the purchase price paid for the business was approximately \$10 million dollars less than the net book value of the assets on Capital's books and (2) that at the time of purchase, the rail properties were valueless (J. A. 219).

The record, however, contains testimony by Transit's witness that in purchasing the business no such risks or liabilities were assumed by the investors, and that the rail properties were far from valueless at the time they were acquired (J. A. 239-242). In addition, witness Falk testified that if the Harris theory were adopted, the rate and depreciation bases would have to be increased to include the additional amount of the obligations allegedly assumed under that theory (Appendix to this Brief, 26-27).

It is obvious from the opinion (J. A. 15-18) that witness Harris' theory received the attention of the Commission, and, for ample reasons, was not adopted. The Commission's action in this respect denotes its rejection of the contention that Transit's investors had assumed the risk of obsolescence of rail properties. In considering and rejecting such a theory, and in approving the allowance for depreciation of rail properties and for track removal complained of here, the Commission effectively expressed its conclusion that Transit's investors did not assume a risk of obsolescence of such

properties, and have not been otherwise compensated therefor.

(2) Bus properties

Appellants have further questioned the propriety of the amount of the Commission's allowance for depreciation insofar as it relates to Transit's bus properties.

Title 43, Section 315 of the District of Columbia Code, 1951 Ed. provides as follows:

"Every public utility shall carry a proper and adequate depreciation account. The commission shall ascertain and determine what are the proper and adequate rates of depreciation of the several classes of property of each public utility. These rates shall be such as will provide the amounts required over and above the expense of maintenance to keep such property in a state of efficiency corresponding to the progress of the industry. Each public utility shall conform its depreciation accounts to such rates so ascertained and determined by the commission. The commission may make changes in such rates of depreciation from time to time as it may find to be necessary. The commission shall also prescribe rules, regulations, and forms of accounts regarding such depreciation which the public utility is required to carry into effect. The commission shall provide for such depreciation in fixing the rates, tolls, and charges to be paid by the public."  
(Emphasis Supplied)

Accordingly, the Commission is vested with complete control over the matter of depreciation rates. In its Order No. 4001, of May 29, 1953, (J. A. 73-74), the Commission required the use of the group method of depreciation for buses. Under this technique, which is extensively used in utility regulation, depreciation rates are based upon the average

service life of the property in question. Appellants' argument that the Commission depart from its long-established group method of depreciating buses and adopt the unit method is patently without substance. The Commission's reasons for electing not to adopt the unit method are clearly and adequately set forth in its opinion (J. A. 15, 17-18).

Although it is true that the group method of depreciation had resulted in depreciation accruals in excess of original cost on certain over-age buses, the staff of the Commission recommended that there be no change in such group method but that any excess accruals applicable to such buses should be applied as a partial offset to any unrecovered depreciation relating to rail facilities. The Commission adopted the staff recommendation. Under the broad discretionary powers granted to the Commission in the above-quoted statute, the Commission was fully justified in retaining the excess accruals for application against possible unrecovered depreciation of rail facilities. Moreover, even without reference to the rail facilities accounts, the powers granted the Commission were more than sufficient to justify the Commission's action in continuing to use the same group method of depreciation.

Under the circumstances and particularly in the light of the above-quoted statute, the action of the Commission was hardly unreasonable, arbitrary or capricious. Its decision has a clearly rational basis, and the fact that some other course of action might have been selected is immaterial. American

Power & Light Co. v. Securities and Exchange Commission, 329  
U. S. 90, 118 (1946).\*

F. Appellants' Allegations of Other  
Errors are Totally Without Merit.

Appellants' concluding argument charges that the Commission "committed other errors in this proceeding" (Appellants' Brief, pp. 68-70). Appellants state that in 1959 Transit's parent corporation underwent a reorganization, and that during the same year Transit's "grandparent" (Transportation Corporation of America), engaged in selling the stock of Transit's "parent" corporation (D. C. Transit System, Inc., a Delaware corporation). There was absolutely no showing on the record by Appellants that the matters referred to had any relevance at all to this proceeding. Moreover, Appellants have not introduced any evidence or otherwise explained the supposed wrongdoing which arises from these facts.

Appellants imply also that there is something improper in the fact that Transit keeps a portion of its cash deposits in New York City banks. Although Appellants' allegations are wrought with innuendos, they make not even the slightest showing that Transit's banking policies or practices are in any way improper.

Appellants then contend that the Commission erred in excluding evidence as to whether officials and stockholders

\* It is further worth noting that the Commission indicated its intent to make a complete study of the status of the existing depreciation reserve with respect to all Transit's depreciable property (J. A. 15, 18).



of Transit and its "parent" and "grandparent" companies are "obtaining benefits" from Transit's New York City depositories. A reference to their citation of the record (J. A. 242-243), indicates that the ground on which the Commission sustained Transit's objection to a question covering this point was that the question was improper cross examination of Transit's rebuttal testimony since it was beyond the scope of such rebuttal testimony, and since the record prior thereto had contained no evidence of any kind on the subject of the bank deposits. Moreover, in making its ruling, the Commission advised Appellants that cross examination of rebuttal testimony which itself was unrelated to bank deposits was an inappropriate way to present any evidence Appellants might wish to present on the subject. Appellants were not precluded from presenting their own evidence on the subject, if they had any. The Commission's ruling on this objection was clearly correct.

Finally, in a footnote on page 70 of their Brief, Appellants state that "Subsequent to the hearing it was learned by plaintiffs that Transportation Corporation of America issued \$1,100,000 of 5 1/2% Convertible Subordinated Debentures and that the Trustee under the Indenture was a bank in which Transit maintains deposits." This reference by Appellants is highly improper since there is nothing in the record concerning this matter. Appellants include this reference to raise the inference that because of Transit's deposits, its "parent" companies receive favorable consideration by the bank in question on loan applications (Appellants' Brief, p. 17). The fact is, however, that the loan referred to was

one made not by the bank itself but by the purchasers of the debentures, i.e., the members of the investing public. The bank merely served as Trustee under the Indenture securing the loan, for which the bank receives its standard nominal fee. Absolutely no inference of wrongdoing can be raised from this transaction.

## II

THE QUESTIONS RAISED BY APPELLANTS  
HAVE BEEN RENDERED MOOT AS A RESULT  
OF COMMISSION ORDER NO. 4735, DATED  
JANUARY 18, 1961

The Order complained of on this appeal (Order No. 4631, dated March 2, 1960, J.A. 4, the "1960 Order") has been superseded by a subsequent Order of the Commission (Order No. 4735, dated January 18, 1961, excerpts from which are included at pp. 13-15 of the Appendix to this Brief, the "1961 Order").\* An extensive opinion in support of the Commission's 1961 Order may be found at 38 P.U.R. 3d 19 (1961), In the Matter of D. C. Transit System, Inc.

In brief, the 1961 Order and opinion thereto show that on September 14, 1960 Transit filed with the Commission a revised rate schedule. The Commission suspended this revised rate schedule and ordered a hearing and investigation thereon.

\* This Court may, of course, take judicial notice of this subsequent action by the Commission. Washington Gas Light Co. v. Baker, 195 F.2d 29 (D. C. Cir., 1951).

Formal public hearings on Transit's petition were conducted on thirteen days during the period from September 29, 1960 to January 4, 1961, inclusive. Two company witnesses and one independent expert testified on behalf of Transit. Two witnesses testified on behalf of the Commission, and four witnesses testified on behalf of the intervening citizens associations and/or the individual intervenors. In addition, a number of representatives of the public appeared in person and made statements. Written statements were submitted by others and made a part of the record. The total record made before the Commission consisted of 2,014 pages of testimony and 74 exhibits.

Thereafter, in the 1961 Order, the Commission denied Transit's petition. On the basis of the record in that proceeding, it was found by the Commission:

"That the present District of Columbia Schedule of Rates \*\*\* is just, reasonable, and compensatory and will enable the Company to meet its obligations, to maintain a sound financial structure, to reasonably compensate investors, and to furnish service adequate to meet the growing needs of the community."  
(1961 Order at p. 15 of the Appendix to this Brief)

Accordingly, it was ordered that the then-existing schedule of rates remain in effect. As a result of the 1961 Order, the question of the propriety of Transit's 1960 Rate Schedule complained of herein should no longer be considered by the Court.

The 1961 Order rests on its own record, a record entirely independent of that underlying the 1960 Order. An examination of the findings and conclusions contained in the later Order, and of the Commission's opinion in support thereof, demonstrates that in January 1961 the basis for the Commission's action differed materially from that relied upon in March of 1960.

To illustrate: In the 1959 proceeding the Commission used the twelve-month period ended September 30, 1959 as a past period to test the actual level of earnings, and the twelve months ending December 31, 1960 as the test period for estimating the company's level of earnings for a future period. (J. A. 1) In the 1960 proceeding, however, the six months ended August 31, 1960 were used as the proper past test period, and the twelve months ending February 28, 1961 were used as the proper future test period (1961 Order at p. 15 of the Appendix to this Brief). Consequently, in the 1960 proceeding, evidence of and estimates of revenues and expenses related to periods subsequent to those employed in 1959, and the Commission's basis for judgment differed materially from that relied upon in the 1959 proceeding.

The 1961 Order speaks as of, and from, the date of its promulgation by the Commission, January 18, 1961. It is on the authority of this Order, not of the 1960 Order, that Transit's present schedule of rates is effective within

the District of Columbia.

Thus, Title 43, Section 707 of the District of Columbia Code, 1951 Ed., specifically provides that:

"All orders and decisions of the Commission shall remain in full effect, \*\*\* unless and until they are suspended, superseded or rescinded by the Commission or are vacated by lawful order of the District Court of the United States for the District of Columbia \*\*\*."

Title 43, Section 703 of the District of Columbia Code, 1951 Ed., further states that:

"All rates, tolls, charges, time and condition of payment thereof, schedules and joint rates fixed by the Commission shall be in force and shall be prima facie reasonable until finally found otherwise in an action brought for that purpose."

Finally, Transit's Franchise declares in Section 5 that:

"If the Commission suspends [a] new schedule it shall immediately give notice of a hearing upon the matter and, after such hearing and within such suspension period, shall determine and by order fix the schedule of rates to be charged by the Corporation"

Consequently, there can be no doubt that rates charged by Transit since January 18, 1961 and currently in effect in the District of Columbia have been established and are governed by the 1961 Order.

Since the 1960 Order has been superseded, and because the reasonableness of the 1961 Order is not now before this



Court, it is plain that the major issue herein is moot and that, even if the Court adopted Appellants' arguments, no practical relief could or should be afforded Appellants.

Since any determination of this Court in Appellants' favor would be largely ineffectual, this appeal should be dismissed. It is axiomatic that this Court should concern itself only with actual controversies and that it is not within its province to decide abstract, hypothetical questions from the determination of which no practical relief can follow. Board of Public Utility Commissioners v. Componia General De Tabacos De Filipinas, 249 U.S. 425 (1918); Fleming v. Munsingwear, Inc., 162 F.2d 125, 128 (8th Cir., 1947); Fleming v. Knudson & Mercer Lumber Co., 159 F.2d 212 (7th Cir., 1947); Spreckels Sugar Co. v. Wickard, 131 F.2d 12 (D. C. Cir., 1941). For example, in the Munsingwear case the issue was the propriety of certain prices charged by the Munsingwear Company. The District Court found the Company's prices to be proper and dismissed the complaint of the Office of Price Administration. An appeal was taken and during the pendency of the appeal, prices on the commodities involved were decontrolled. Despite the fact that the outcome of a treble damage action apparently turned on its decision, the Court of Appeals dismissed the case as moot, noting that it would "concern itself only with actual controversies" (p. 128).

It is true that Appellants request the Court to order Transit to account for its revenues subsequent to March 6, 1960 in the event that Appellants prevail on this appeal (Appellants' Brief, p. 71). But, we have already shown this



Court does not have it within its power to require Transit to account for revenues subsequent to January 18, 1961, since Transit's rates in force after that date are based on the 1961 Order. Nor should this Court compel such an accounting even for the interim period from March 6, 1960 to January 18, 1961.

The accounting that Appellants here seek is as to rates declared just and reasonable by a rate making Commission empowered by Congress to set rates. Transit is required under penalty of law to charge and collect such rates. Title 43, Section 902 of the District of Columbia Code, 1951 Ed. Under the circumstances, a finding of error in the administrative order would not constitute sufficient grounds to order a refund or accounting. A refund or accounting under these facts is a matter of restitution - and restitution is not a matter of right, but ex gratia, Atlantic Coast Line RR. Co. v. Florida, 295 U.S. 301, 309-310 (1934).

We contend, furthermore, that there can be no equity in requiring a utility to refund a rate established by a commission that has jurisdiction to regulate rates when the utility must collect the rates under penalty of law. This contention is supported by a well-reasoned decision rendered by the Supreme Court of Illinois in 1954. In Mandel Bros., Inc. v. Chicago Tunnel Terminal Co., 2 Ill. 2d 205, 117 N.E.2d 774 (1954), the utility filed a schedule of increased rates with the

Illinois Commerce Commission. The Commission initially suspended the rates, but, then, after hearing, ordered the utility to put them into effect. Thereafter, the Illinois Circuit Court, on review brought by a shipper, reversed the order of the Commission. The shipper then sought reparations before the Commission. The Commission denied reparations, and the shipper once again sought review in the Circuit Court, which once again reversed the order of the Commission. On further appeal by the utility, the Supreme Court of Illinois reversed the Circuit Court, saying (117 N.E.2d, pp. 776-777):

"On such hearing the commission shall establish the rate \*\*\* which it shall find to be just and reasonable." (Ill. Rev. Stat. 1953, Chap. 111-2/3, par. 36). By section 37, a public utility is prohibited from charging 'a greater or less or different compensation,' than the rate so approved by the commission. (Ill. Rev. Stat. 1953, Chap. 111-2/3, par. 37). For failure to charge the approved rate a public utility is subjected to the severe penalties prescribed by section 76, Ill. Rev. Stat. 1953, Chap. 111-2/3, par. 80."\*

\*\*\*\*\*

"It follows that the rate approved by the Commerce Commission as just and reasonable was the rate which the utility was required to charge so long as the order of the commission remained in effect. It cannot be said that in charging that rate the utility charged an excessive rate which gave rise to a claim for reparations. It follows that the judgment of the circuit court must be reversed and the Order of the Commerce Commission confirmed."

\* These provisions of the Illinois Revised Statutes are comparable with the following provisions of the District of Columbia Code: Title 43, Sections 401, 408, 707 and 906, 1951 Ed.

The Mandel case was relied upon in Keco Industries, Inc. v. Cincinnati & Suburban Bell Telephone Co., 166 Ohio 254, 18 P.U.R. 3d 108 (1957), app. dismd. and cert. den., 355 U.S. 182 (1957). In that case, pursuant to a statutory scheme like the one here present, it was held that the setting aside on appeal of a rate order furnishes no right of action for restitution in the absence of a statute specifically granting such a remedy, since the rates collected were the lawful ones at the time of collection and were, in fact, the only ones that the utility could properly collect.

We recognize, of course, that this Court in Washington Gas Light Co. v. Baker, 188 F.2d 11 (D. C. Cir., 1950), cert. den., 340 U.S. 952, did in 1950 require a refund of a rate established by the Commission. However, in that case this Court was careful to note that:

"Pending disposition of the appeal, this Court ordered 'the amount hereafter received by the Washington Gas Light Company under the increase' set aside subject to future order of the Court." (p. 14)

No such order exists in this case. Moreover, in Baker no question concerning the propriety of the refund was raised. The Commission had granted Washington Gas Light Co. a rate increase. This action was reversed by the District Court and the Company moved for a stay so as to keep the increase in force pending its appeal to the Court of Appeals.

The stay was granted, and the Company acquiesced in an Order directing that the increase be placed in a special fund.

Baker thus presents facts completely unlike those before the Court and is hardly authority for a retroactive accounting or refund in this proceeding.

Refunds, it is true, have been ordered in other cases in which commissions lacked jurisdiction to set or permit the rate in question. United Gas Pipe Line Co. v. Mobile Gas Service Corp., 350 U.S. 332, 347 (1956). And refunds have, of course, been ordered of rates kept in effect by a stay during judicial review of a commission's order establishing lower rates. See, e.g. Federal Power Commission v. Interstate Natural Gas Co., 336 U.S. 577 (1948); Pennsylvania Water & Power Co. v. Federal Power Commission, 193 F.2d 230 (D. C. Cir., 1951), *affd*, 343 U.S. 414 (1952). But these cases are on their facts manifestly different from the one now before the Court.

Nor can it be urged that this Court should reach the merits of this case on the ground that its determination would provide future guidance for the regulation of Transit by the Commission, since the functions of the Commission have been assumed by the newly created Washington Metropolitan Transit Commission, which will operate pursuant to an interstate compact between the District of Columbia, Virginia and

Maryland (approved by joint resolution of Congress, Act of September 15, 1960, 74 Stat. 1031). Any determination in this proceeding would be of doubtful value as a guide to future proceedings brought under such interstate compact.

Accordingly, it is plain that even if this Court were inclined to decide this case in Appellants' favor, it should not do so since it can grant Appellants no effective relief: The rates presently in force would remain in force pursuant to the 1961 Order and no refund or accounting is appropriate in this case. Nor would a determination in Appellants' favor serve any other useful purpose.

Transit respectfully submits, therefore, that this appeal should be dismissed on the ground that the principal issue herein is moot and that Appellants' proper remedy is to pursue an appeal from the 1961 Order.\*

### III

#### Conclusion

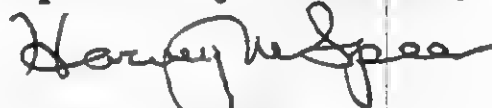
Transit submits that (1) the Commission's Order was amply and fully supported by the findings, opinion and record, and was in no sense arbitrary, capricious or unreasonable and that (2) in any event, the question of the propriety

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\* Such an appeal is presently pending before the District Court and Appellant Bebchick is there contending that the Commission erred in the 1961 Order in failing to reduce Transit's 25¢ cash fare to 20¢ (Appellants' Brief, p. 22). The outcome of that appeal, unlike the outcome of this one, could grant Appellants substantial relief, since it could, if decided in Appellants' favor, result in a reduction in Transit's fare.

of Transit's present rates is not before the Court and that the principal issue herein is moot. Accordingly, the appeal should be dismissed and the order of the District Court should be affirmed.

Respectfully submitted,



HARVEY M. SPEAR  
OWEN J. MALONE  
3600 M Street, N. W.  
Washington 7, D. C.

Dated:  
November 29, 1961



A P P E N D I X

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

March 31, 1960

IN THE MATTER OF	)	
	)	
Petition of D. C. TRANSIT SYSTEM, INC.	)	P. U. C. No. 3628
For Change in Schedule of Rates.	)	Formal Case No. 471

OPINION IN SUPPORT OF  
FINDINGS, CONCLUSIONS, AND ORDER  
PROMULGATED MARCH 2, 1960  
(Order No. 4631)

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Test Periods for Determining Level of Earnings

In the presentation of its case, the Company used the twelve months ended September 30, 1959, for determining its actual level of earnings for a past test period and the twelve months ending December 31, 1960, for measuring its estimated level of earnings for a future test period.

No issue was raised by any party to the proceedings with respect to the test periods above noted. The witnesses for the staff and intervenors also used these periods for purposes of their testimony and exhibits. We find that the twelve months ended September 30, 1959 offer the latest practicable test period available to determine the Company's actual level of earnings, and that the calendar year 1960 is an appropriate period to be used for forecasting operating results for the future, after giving effect to appropriate adjustments for changes in the level of revenues and expenses.

The nature of the Company's application, whereby it requested the Commission to approve at this time two increases in fare, the first to become effective immediately, and the second to become effective approximately one year in the future, is, insofar as we have been able to determine, unique in the annals of regulatory practice. In support of its request for a second increase in fares the Company offered testimony and exhibits based upon projected operating results for the calendar years 1961 and 1962.

We believe that the operating and economic uncertainties of the transit industry in general, by reason of the trend of decline in passengers and increase in operating costs, are such as to render long range prophecies of little value as a basis for fixing rates. More particularly, the evidence of record in this case clearly demonstrates

that where a Company is in the throes of a major conversion from street railway to bus operation, guide lines are virtually nonexistent. While it is not unusual in regulatory practice to forecast operating results for a reasonable period as a basis for fixing rates, we know of no precedent, nor does the record in this case establish, any valid basis for the forecasting of operating results for more than one year in the future. Accordingly, the Commission finds that the estimates of operating results for the years 1961 and 1962 are not sufficiently reliable to serve as a basis for providing, at this time, for an increase in rates to become effective November 1, 1960, as proposed by the Company and therefore estimates of operating results for a period beyond December 31, 1960 should be rejected.

#### NET OPERATING INCOME

Three witnesses presented testimony and exhibits showing estimated net operating income for the future test period, twelve months ending December 31, 1960, at present fares, as follows:

	<u>Total Operations</u>	<u>Mass Transportation Operations<sup>5</sup></u>
Witness Flanagan for the Company (Exhibit No. 10-A) <sup>6</sup>	\$218,875	\$ 265,621
Witness Falk for the staff of the Commission (Exhibit No. 39)	\$586,192	\$ 660,146
Witness Harris for the intervenors (Exhibit No. 54-A)	\$ —	\$1,141,273

Based on their respective calculations, Flanagan and Falk both testified that the Company was entitled to some increase in rates, although in substantially different amounts. Harris testified that on the basis of his estimate of net operating income shown above, which is after provision for payment of motor vehicle fuel taxes, the return at present fares would be at such a level as to warrant no increase in fares at this time.

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<sup>5</sup>After excluding estimated net deficits from limousine operations and from charter and sightseeing operations.

<sup>6</sup>After adjustment for errors in original Exhibit No. 10 showing net operating income of \$101,016 and \$165,413 respectively. Related exhibits were similarly adjusted.

Both the Company witness and the staff witness used as a starting base for their projection of revenues and expenses for the future test period figures for the twelve months ended September 30, 1959, as recorded on the books. Adjustments were made to a going level basis to give effect to changes in the level of revenues and expenses that were in effect for only a portion of the twelve-month period ended September 30, 1959, and also for known changes in expenses that would be in effect for all or a portion of the twelve months ending December 31, 1960. A comparison of the difference in net operating income applicable to total operations, prior to allocation to limousine operations and to charter and sightseeing operations, together with the differences in the various adjustments proposed by the two witnesses, are summarized and discussed hereafter.

	Company Witness (Exhibit No. 10-A)	Staff Witness (Exhibit No. 39)	Differences
Operating Revenues	<u>27,661,524</u>	<u>\$ 27,661,524</u>	<u>\$ --</u>
Operating Revenue Deductions:			
Operating expenses	23,446,444	23,292,023	154,421
Taxes, other than income taxes	751,892	738,570	13,322
Income taxes	246,096	343,432	- 97,336
Depreciation	2,987,925	2,691,015	296,910
Amortization of acquisition adjustment	- 1,033,904	- 1,033,904	--
Provision for track removal and repaving	<u>1,044,196</u>	<u>1,044,196</u>	<u>--</u>
Total	<u>27,442,649</u>	<u>27,075,332</u>	<u>367,317</u>
Net Operating Income	<u>\$ 218,875</u>	<u>\$ 586,192</u>	<u>\$ -367,317</u>

(a) Operating Revenues

It will be noted from the above that there is no difference in the estimates of operating revenues by the two witnesses. Both estimates reflect a reduction in revenues from Government contract operations in the amount of \$106,014 by reason of the loss of certain Government contract work effective as of July 1, 1959. Other operating revenues were increased by \$35,220 to give effect to an estimated increase in rental revenues from certain of the Company's properties which were leased out for only a portion of the twelve months ended September 30, 1959. We find that \$27,661,524 represents a reasonable estimate of operating revenues at present fares for the twelve months ending December 31, 1960.

(b) Operating Expenses

The adjustments to operating expenses proposed by the two witnesses are summarized as follows:

	<u>Company Witness</u>	<u>Staff Witness</u>	<u>Difference</u>
Increased labor costs based on changes in labor rates during the twelve months ended September 30, 1959	\$ 297,267	\$ 297,267	\$ --
Increased labor costs and related fringe benefits based on changes subsequent to September 30, 1959	672,284	672,284	--
Reduction in provision for Injuries and Damages based on the net reduction in operating revenues	- 3,009	- 3,009	--
Reduction to exclude improper charges to operating expenses	- 9,958	- 34,800	- 24,842
Reduction in expenses related to reduction in Government contract operations	- 75,731	- 76,982	- 1,251
Reduction in expenses related principally to conversion from rail to bus operations on January 3, 1960	<u>-579,775</u>	<u>-708,103</u>	<u>-128,328</u>
Net Increase in Expenses	\$ 301,078	\$ 146,657	\$ 154,421
	<u>=====</u>	<u>=====</u>	<u>=====</u>

The reduction for improper charges to operating expenses proposed by the staff in excess of the adjustment proposed by the Company witness represents expenditures during the years 1957 and 1958, principally for architectural fees, in connection with planning for the construction of terminal buildings and bus shelters. The staff witness testified that no construction has been undertaken up to the present time, and that if and when construction is undertaken, all or some portion of these charges might be properly charged to fixed capital accounts, but they would not, in his opinion, constitute a proper charge to operating expenses under any condition. The witness for the Company predicated the charge to operating expenses on the basis of the expenditures being in the nature of development costs in the interest of improved service, and on the assumption that the terminals would produce operating revenues to the benefit of the riding public. We cannot accept either of the reasons advanced by the Company witness as justifying, under sound regulatory accounting, the charge to operating expenses. We find that the adjustment proposed by the staff witness to exclude \$24,842 from operating expenses is a proper adjustment.



The difference of \$1,251 in the two estimates for the reduction in operating expenses related to the reduction in Government contract operations is so minor that the estimate of either witness could be accepted as reasonable. The Company did not question the propriety of the slightly higher estimate proposed by the staff witness, and we will accept his adjustment with respect to this item.

It will be noted that there is a substantial difference in the estimates of the two witnesses of the savings that will be realized by reason of the reduction in rail operations and the partially offsetting increase in bus operations resulting principally from the conversion of the three street car lines to bus operations on January 3, 1960. The Company witness estimated a net reduction in over-all expenses during the year 1960 of \$579,775, while the staff witness estimated a net reduction of \$708,103, or a difference between the two estimates of \$128,328.

As shown by Schedule 1-A of Exhibit No. 10-A, the Company witness estimated that rail operating expenses would be reduced in the total amount of \$2,021,641 based on a reduction of 431,440 car hours, times the cost per hour of certain items of expense considered to vary directly in relation with the reduction in car hours. Correspondingly, bus operating expenses were increased by \$1,441,866 based on an estimated increase of 340,095 bus hours. Under this procedure a number of items of expense were not affected by the conversion of the three lines on January 3, 1960.

The record shows that, based on Exhibit No. 10 as originally presented by the Company, rail hours were reduced by 43.6% while rail operating expenses were reduced by only 24.1%. Correspondingly, bus hours were increased by 15.3%, whereas bus expenses were increased by only 9.3%. Under questioning by staff counsel with respect to these substantial variations in the percentages of change in the number of hours operated and the related expenses, the witness for the Company stated that he had followed the same procedure that has been followed for many years in rate proceedings before this Commission in adjusting for changes in the level of expenses incident to reduced operations. He made no distinction between adjusting for minor variations in the level of operations from year to year and, as in this case, a major shift of approximately 50% of existing rail operations to bus operations. He further stated that no effort was made to adjust other elements of cost beyond that shown by his exhibit by reason of his inability to estimate accurately the extent of such change until there has been complete conversion of the rail operations.



The staff witness, as shown by Sheets 5 and 6 of Schedule 1, Exhibit No. 39, estimated that there would be a reduction of \$3,716,981 in rail operating expenses with a partially offsetting increase in bus operating expenses in the amount of \$3,008,878. These estimates give effect not only to expense items that would be reduced by reason of the substitution of buses for street cars, but also to expense items that were transferred from rail operations to bus operations, even though no change in the amount of the expenses would result. The witness testified that unless this procedure is followed, unit costs to be used as a basis for allocating bus operating expenses to charter and sightseeing operations would be understated. This is so by reason of relating bus hours or bus miles which give effect to the January 3rd conversions to expenses that were not fully adjusted for the effect of such conversions.

The Company took particular exception to the staff adjustment reducing the item of rail operating expenses for maintenance of way and structures by \$229,488, or from \$464,549 to \$235,061. Under the Company proposal the estimated cost of maintenance of way and structures would remain at \$464,549 even though there has been an abandonment of approximately 50% of existing rail facilities. The record shows that the Company's budget for 1960 includes \$320,000 for the item of maintenance of way and structures. This amount is \$144,000 less than the estimate included in the Company exhibit.

We recognize that precise estimates cannot be made of changes in operating expenses as a result of conversion. On the other hand, we cannot accept as reasonable the Company contention that because the effects of conversion cannot be precisely measured at this time, no effort should be made to arrive at a reasonable estimate of same. We are of the opinion that the proposal by the staff witness represents a reasonable estimate, and that the estimated reduction of \$708,103 in operating expenses related principally to the conversions from rail operations to bus operations which took place on January 3, 1960, is a proper adjustment and should be adopted.

The intervenors proposed no adjustments to operating expenses and adopted the adjusted expense figures shown by the staff exhibits.

Based on the foregoing, we find that operating expenses in the amount of \$23,292,023 applicable to the twelve months ending December 31, 1960, prior to allocation to limousine operations and to charter and sightseeing operations, represents a reasonable estimate of such expenses for purposes of this proceeding.

**(c) Taxes, Other Than Income Taxes**

As heretofore shown, the difference in taxes, other than income taxes, as estimated by the witnesses Flanagan and Falk, amounts to only \$13,322. There was complete agreement by the two witnesses with respect to the following adjustments:

Increase in payroll taxes based on increased labor costs	\$105,351
Increase in payroll taxes based on increased F.I.C.A. tax rates and taxable base	44,310
Adjustment to exclude credit for overaccruals in operating taxes in prior years	8,217
Adjustment to include estimated liability for motor vehicle fuel taxes applicable to limousine and charter operations	<u>10,193</u>
Total	<u>\$168,071</u>

In addition to the foregoing adjustments, the Company witness reduced payroll taxes in the amount of \$2,984 based on a reduction in labor charges related to the reduction in Government contract operations heretofore referred to. A similar adjustment was proposed by the staff witness in the amount of \$1,680, or \$1,304 less than the adjustment proposed by the Company witness. The staff witness also proposed an adjustment reducing payroll taxes by \$14,626 based on the estimated reduction in labor costs incident to the conversion from rail to bus operations. No similar adjustment was proposed by the Company witness. No exception was taken to the accuracy of the last two adjustments proposed by the staff resulting in a net difference of \$13,322 in operating taxes as estimated by the two witnesses.

The witness for the intervenors proposed an adjustment to reduce estimated payroll taxes as developed by the staff witness, after allocation to charter and sightseeing operations, by \$41,443. The basis for this adjustment is not entirely clear from the record, but it is apparent that the adjustment proposed by this witness does not give proper consideration to the estimated increase in payroll taxes resulting from an increase in the taxable wages for F.I.C.A. purposes from \$4,200 to \$4,800. Accordingly, we cannot accept the adjustment proposed by the intervenors' witness.

Based on the foregoing, we find that operating taxes, other than income taxes, for the twelve months ending December 31, 1960, in the amount of \$738,570, prior to allocation to limousine operations and to charter and sightseeing operations, represents a reasonable estimate for purposes of this proceeding.

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(c) Income Taxes

The summary of net operating income heretofore set forth shows that income taxes under the staff proposal exceed income taxes under the Company proposal by \$97,336. This difference is primarily attributable to the effect on income tax accruals of the adjustments to operating expenses and taxes, other than income taxes, proposed by the staff witness in different amounts from those proposed by the Company witness. The record shows the adjustments made by the staff witness to corporate net income to arrive at net taxable income. Since we have accepted the adjustments proposed by the staff witness heretofore discussed, we also accept as proper his accruals for income taxes in the amount of \$343,432 prior to allocation to limousine operations and to charter and sightseeing operations.

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## PROPOSED FARE STRUCTURES

On November 6, 1959, the Company filed two schedules calling for increases in rates, the first of which was to become effective on November 16, 1959, and the second to become effective November 1, 1960, and requested approval by the Commission of both schedules at this time.

The first schedule proposed by the Company is a unique fare structure of 25 cents cash during rush hours and a 20 cent cash fare during non-rush hours, with school fares remaining at 10 cents. The rush hours were defined as those periods between 6:00 A.M. and 9:30 A.M. and between 3:30 P.M. and 7:00 P.M. on Mondays through Fridays inclusive, except for U. S. Government holidays. During all other times the adult District of Columbia fare was to be 20 cents. Under the second schedule, the 20 cent non-rush hour fare would be increased to 25 cents, so that the adult District of Columbia fare would then be 25 cents cash at all times.

With respect to the second schedule of fares which the Company proposes to become effective on November 1, 1960, we have heretofore found that the estimates of operating results for the years 1961 and 1962 are not sufficiently reliable to serve as a basis for an increase in rates to become effective twelve months in the future. Having so found, we conclude that the fare structure proposed by the Company of a 25 cent cash fare and a 10 cent school fare to become effective November 1, 1960, must be rejected.

With respect to the first schedule, the reason advanced by the Company for the higher rush hour fare was that it experiences the greatest amount of operating expenses during rush hour periods and therefore the riders during such periods should pay a higher fare. While it is true that expenses are at their highest level during rush hours, it is also true that the greatest number of riders use the Company's vehicles during those hours. The record shows that 60% of the passengers ride during the rush hour periods, or during 21% of the total hours per week. The Commission is of the opinion that the Company has failed to demonstrate that the cost per rider is greater during rush hours than during non-rush hours. Accordingly, we find no justification for a surcharge during rush hours.

Staff witness Edward A. Roberts, a recognized expert in the field of transportation, testified that practically the entire increase sought under the Company's first schedule of fares would be borne by the regular riders and that the casual riders, most of whom use the service only during non-rush hours, would enjoy a substantially lower fare than the regular riders. In the opinion of the Commission this differential in fares would be discriminatory. Other undesirable features of the Company's proposal are that it would tend to discourage patronage by the regular riders and it would require a change in fares four times during each weekday. This latter feature would inevitably give rise to differences of opinion between passengers and drivers at the time of each fare change. The Commission is of the opinion that both features would adversely affect public relations and would undoubtedly result in some loss in patronage and some deterioration in service.

We note that although the Company argues that rush-hour passengers should pay a higher fare than non-rush hour passengers, it negates its own argument by proposing to abandon such a fare structure in less than a year. We refer, of course, to the second part of the Company's application which asked for approval of a fiat 25 cent adult cash fare at all times, beginning November 1, 1960. The record fails to show that any transit company is presently authorized to charge a premium fare during rush hours. It is true that certain incentives to promote non-rush hour riding have been tried by various companies, but an off-peak promotional rate is quite different from a premium rate during rush hours.

The fare structure proposed by the staff consists of a 25 cent cash fare, a token fare of 20 cents, with tokens to be sold in units of 5 for \$1.00, and a school fare to remain at 10 cents. Under this fare structure, the regular riders who buy tokens would not incur any increase in fares, and the major portion of the increase in revenues would be derived from the casual riders. Another advantage of this fare structure is that it would reduce the number of money transactions with the operators to a minimum and would, therefore, in our opinion, tend to speed up the service.

Exhibit No. 30 shows that of the fare structures in the 30 largest cities in the country, 17 have a cash fare combined with a reduced token fare, with three of the cities having the same fare structure as that proposed by the staff in this proceeding. Ten of those cities have a 25 cent cash fare, but no city has a fare structure employing a premium fare during rush hours, as proposed by the Company in its first schedule.

The Company estimates that its fare structure will produce additional revenue of \$1,907,131, while witness Roberts calculates that a more realistic appraisal of the Company's fare structure would result in additional revenue of \$2,588,176.

In reaching the estimated increased revenue of \$1,907,131, witness Flanagan testified that in his opinion 10% of the rush-hour passengers would shift to non-rush-hour periods in order to save 5 cents per ride. Witness Roberts testified that his analysis of the passenger counts during 15-minute periods indicated that the maximum shift that reasonably could be expected was no more than 5%. To illustrate his reasoning, Roberts pointed out that the shift in riding habits to save the 5 cents could be expected to come almost entirely from those passengers riding during the half-hour periods at either end of the rush hours. He then showed that if all of the riders during the first and last quarter hours of the rush-hour periods were to shift, it still would not amount to 10% of the rush-hour passengers. Flanagan offered no support for the 10% shift he anticipated, other than his judgment. The Commission is of the opinion that the estimate of witness Roberts, supported by his studies, is more realistic and that a shift of not more than 5% could be expected.



To compute the loss of passengers that would result from resistance to the increase in fares, witness Flanagan applied a shrinkage or resistance factor of  $.33\frac{1}{3}\%$  for each 1% increase in fare, with a resultant loss of 8.333% of the remaining rush-hour riders, or a loss of 5,448,572 passengers. Witness Roberts testified that on the basis of his studies, he was of the opinion that the loss in passengers from the fare increase would be no more than 5%, or 3,450,900 passengers. This is at the rate of .20% for each 1% increase in fare. In support of his opinion, he pointed out that the resistance to the 1958 increase in rates of D. C. Transit was negligible, even though the Company had used a shrinkage factor of  $.33\frac{1}{3}\%$  in that case, as in this case. He also pointed out that the national average of shrinkage factors in cities over 500,000 was 25%, with a range of .15% to .31%.

Witness Flanagan's opinion as to a loss of 8.333%, or  $.33\frac{1}{3}\%$  for each 1% increase in fare, was supported by an expert witness for the Company, John F. Curtin. This witness, who is well known as an advocate of the  $.33\frac{1}{3}\%$  shrinkage factor, testified that he would recommend this factor as applicable to any transit company, wherever it might be located, and that he could make such a recommendation from his office in Philadelphia. In support of his theory, Curtin offered an exhibit which listed the shrinkage factors resulting from approximately 70 rate changes dating from 1950 to 1958 in various cities throughout the United States. The Curtin study shows no separation of the shrinkage factors found to exist in communities with different population counts, while the Roberts exhibit classifies the shrinkage factors in three groups, those communities of over 500,000 in population, communities with populations of between 100,000 and 500,000, and communities with less than 100,000. It is interesting to note that the combined average shrinkage factor for all communities shown on the Roberts exhibit was .31%, which compares favorably with the Curtin figure of  $.33\frac{1}{3}\%$ , but that for cities over 500,000 it was .25%.

In consideration of the fact that under the Company proposal only the rush-hour rates would be increased, an increase which passengers are least able to resist, and in consideration of the prior experience of this Company in comparison with the national average, it is our opinion that a shrinkage factor of .20% would be appropriate for use in estimating the loss in rush-hour passengers under the fare structure proposed by the Company.

In adopting the shrinkage factor of .25% applicable to the fare structure proposed by the staff, Roberts gave consideration to the population classification of the District of Columbia, as well as to other local conditions. It should be mentioned that Curtin did not include the 1958 D. C. Transit System rate case in his study, and that he was unaware of the shrinkage factor resulting from that increase. It is our opinion that a shrinkage factor giving consideration to local conditions is more reliable than a formula purported to be applicable throughout the United States.

It is also our opinion that the factor of .25% adopted by Roberts for computing the loss in passengers anticipated as a result of the fare structure proposed by the staff is more appropriate than is the factor of  $.33\frac{1}{3}\%$  recommended by Flanagan.

In computing the increased revenue to be anticipated from the adult fare structure of 25 cents cash with 5 tokens for \$1.00, witness Roberts estimated that 70% of the remaining adult passengers would pay the token fare of 20 cents. He based his opinion in part on the experience of other communities where a like fare structure had been in use long enough to develop the actual percentage of token use. His Exhibit No. 53 shows that in the larger communities the token-cash ratio is in the neighborhood of 70%-30%.

Witness Flanagan took issue with the 70% token use and presented testimony which purported to show that a much higher token use would result from the staff's proposal. He estimated that the token use would be between 80% and 90%. The record shows that while Curtin did not testify in this case as to the token use to be expected, he did testify in the Providence case that a fare structure of 25 cents cash with 5 tokens for \$1.00 would result in a token use of 70%, which actual experience proved to be correct. Any estimate of the token ratio at this time must of necessity be based on informed judgment, and can be determined only by actual experience. In our opinion, a token use of between 80% and 90% appears to be unlikely in view of the record in this community and in other communities where a fare structure like that proposed by the staff has been in effect.

Based upon the record, the Commission is of the opinion that a token use of 70% is a reasonable estimate of what may be expected under the fare structure proposed by the staff.

On February 16, 1960, the next to the last day of hearings, the Company presented Exhibit No. 65 which purported to forecast the revenue to be realized from a fare structure of 25 cents cash, tokens at 5 for \$1.10, and a 10 cent school fare. This fare structure differed from that proposed by the staff only in that it made the token rate 22 cents per ride instead of 20 cents per ride, and required the outlay of \$1.10 instead of \$1.00. In computing the resulting revenue, the Company employed a shrinkage factor of .33-1/3% and a token use of 80%. The resulting increase in revenue was estimated to be \$1,951,473. If the shrinkage factor were reduced to .25% and the token use reduced to 70%, the resulting increase in revenue was estimated to be \$2,497,662.

From evidence of record, the Commission is of the opinion that with a differential of 3 cents between cash and token fares and an increase in the cost of the token package to \$1.10, the ratio of token use would be less than 70%, which would result in an even greater increase in revenues than shown above. Each of the amounts set forth above is far in excess of what we hereinafter find that the Company needs to realize a fair return.



From the foregoing, and as shown by Exhibit No. 36, the District of Columbia fare structure proposed by the staff is estimated to produce additional gross revenues of \$1,305,810 on an annual basis. After adjustment is made for comparable increases in fares from the Company's other mass transportation operations, and after consideration is given to the fact that the fare increase could not become effective prior to March 1960, all as shown by Exhibit No. 40, we find that the fare structure proposed by the staff will produce net operating income for the twelve months ending December 31, 1960 in the amount of \$1,143,249, which we hereinafter find constitutes a fair return. Accordingly, we are of the

opinion that a fare structure applicable to mass transportation operations in the District of Columbia, consisting of a 25 cent cash fare, a 20 cent token fare with tokens to be sold in units of 5 for \$1.00, and a 10 cent school fare, affords a practical method of fare collection, and is just, reasonable, and nondiscriminatory.

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PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

Order No. 4735

January 18, 1961

IN THE MATTER OF

Petition of D. C. TRANSIT SYSTEM, INC.  
For change in Schedule of Rates.

}  
P.U.C. No. 3640  
Formal Case No. 474

\* \* \*

FINDINGS, CONCLUSIONS, AND ORDER

D. C. Transit System, Inc. (hereinafter sometimes referred to as the "Company") on September 14, 1960, filed with the Commission a petition for a change in its schedule of rates applicable to the District of Columbia, as follows:

Schedule of Rates - effective November 1, 1960

Cash Fare	-	25¢
Token Fare	-	In units of 4 for 95¢
School Fare	-	10¢, with tickets to be sold in units of 10 for \$1.00 or 20 for \$2.00

By its Order No. 4694, dated September 15, 1960, the Commission, pursuant to Section 5 of Public Law 757, 84th Congress, 2d Session, suspended the proposed schedule of rates for a period of 120 days from the date of filing and ordered that an investigation be made of the subject matter of the petition. In the same Order notice was given that a formal hearing on the petition would be held on September 26, 1960. By its subsequent Order No. 4696, notice was given that the hearing assigned for September 26, 1960, was re-assigned for hearing on September 29, 1960. Leave to intervene was granted to Mount Pleasant Citizens' Association;

Federation of Citizens' Associations of the District of Columbia, Inc.; Public Petitioners, Richard A. Williams, Alfred S. Trask, and Leonard N. Bebhick; Friendship Citizens' Association; and D. C. Federation of Civic Associations.

Formal public hearing was held on 13 days during the period from September 29, 1960 to January 4, 1961, inclusive, resulting in a record consisting of 2,014 pages and 74 exhibits. Testimony was presented for the Company by Parker C. Peterman, Assistant to the President for Finance, and William E. Bell, Superintendent of Schedules and Traffic, both of D. C. Transit System, Inc., and Hawley S. Simpson of the firm of Simpson and Curtin, Consultants in Transportation Engineering; for the staff of the Commission by E. Edward McLean, Chief Accountant, and John L. Ingoldsby, Consulting Engineer; for the intervenor Mount Pleasant Citizens' Association by William A. Roberts, Esq.; for the intervenors Friendship Citizens' Association, Richard A. Williams, Alfred S. Trask and Leonard N. Bebhick; by Harold L. Aitken, Director of Highways and Traffic, District of Columbia, Robert Stromberg, Chief Accounting Officer of Accounting Systems in the Common Carrier Bureau of the Federal Communications Commission; and Alfred S. Trask. In addition, a number of representatives of the public appeared in person and made statements. Written statements were submitted by others and made a part of the record.

\* \* \*

#### Findings and Conclusions

Upon consideration of the entire record in this proceeding, which will be discussed in detail in the supporting opinion hereafter to be filed, the Commission finds and concludes:

1. That the gross operating revenue method should be utilized for measuring rate of return in this proceeding.

2. That the system rate base applicable to mass transportation operations provides a useful means to check the reasonableness of the result obtained from the use of the gross operating revenue method and should be utilized.

3. That the proper past test period for measuring the actual level of earnings, under the circumstances in this case, is the six months ended August 31, 1960.

4. That the proper test period for measuring estimated level of future earnings, under the circumstances in this case, is the twelve months ending February 28, 1961.

\* \* \*

28. That the present District of Columbia Schedule of Rates consisting of a 25-cent cash fare, tokens at 5 for \$1.00, and a 10-cent school fare is just, reasonable, and compensatory and will enable the Company to meet its obligations, to maintain a sound financial structure, to reasonably compensate investors, and to furnish service adequate to meet the growing needs of the community.

NOW, THEREFORE, IT IS ORDERED:

\* \* \*

Section 2. That the present schedule of rates applicable to the District of Columbia, consisting of a cash fare of 25¢, token fare of 5 tokens for \$1.00, and a 10¢ school fare, is just, reasonable, and nondiscriminatory and shall remain in effect.

\* \* \*

A TRUE COPY: |

By the Commission:

Chief Clerk. |

Norman B. Belt  
Executive Secretary

[Transcript pp. 44-45]

By Mr. Spear:

Q. Mr. Flanagan, before testifying in detail as to the exhibits, do you wish to make a statement?

A. [Mr. Flanagan] Yes. some of this may appear repetitious of what my counsel has said. I would like to explain, in a general manner, the necessity which compels the company to seek a change in its schedule of rates at this time. I believe, too, it will be helpful to the Commission if I explain at the outset the considerations which have guided us in the preparation of the presentation of our case.

On October 31, 1959, the representatives of the company agreed with the representatives of Division 689 of the Amalgamated Association of Street, Electric Railway and Motor Coach Employees of America, upon the terms of a three-year contract to run from November 1, 1959 to October 31, 1962. This agreement was reached after extensive and intensive bargaining. The ability of the two parties to arrive at a meeting of the minds precluded the necessity of resorting to arbitration.

The provisions of the new contract will be very costly to the company. Details will be furnished in my later testimony.

[Transcript pp. 44-45, cont.]

We have embarked upon the program of track removal enjoined upon us by Congress. This program entails the removal of streetcar tracks and the repaving of track areas; the abandonment of rail property and streetcars on which the original investment has not been recovered; the expenditure of vast sums of money for the purchase of buses; and the conversion of facilities to make them appropriate for bus operations.

The condemnation of our principal shop for bus maintenance by the District of Columbia Redevelopment Land Agency has made it necessary for us to plan the acquisition of land and the erection of a bus maintenance shop elsewhere, at a cost greatly in excess of the amount realized from the sale of land and property located in Southwest Washington.

[Transcript pp. 383-384]

By Mr. Goodman:

Q. Will the company need any additional investment in 1960?

A. [Mr. Flanagan] It will need very definitely the ability to borrow substantial amounts of money. Its credit must be maintained at a high level.



[Transcript pp. 383-384, cont.]

Q. - - but does the company need the money?  
Does the company need any money?

A. I have testified we are going to buy,  
have already committed ourselves to purchase, 100 new  
buses, to be delivered in the spring.

[Transcript pp. 779-781]

By Mr. Bebachick:

Q. You stated in your testimony at Page 625  
of the transcript:

"This average balance of acquisition  
adjustment is deducted from the depreciated  
original cost of the profits in the second  
column of figures to arrive at the net invest-  
ment in roads and equipment based on purchase  
price."

Would I be correct in assuming from that  
testimony by you that the function of this acquisition  
adjustment, as it has been amortized, is to assure that  
the property, still useful, that was acquired in 1956,  
is valued at the price at which it was purchased? Is  
that the function of this acquisition adjustment?

[Transcript pp. 779-781, cont.]

A. [Mr. Falk] That is the effect of it. The acquisition adjustment when it was set up in 1956 represented the amount by which the original cost of the property exceeded a portion of the purchase price of the assets of the company that was related to the operating property.

Q. That was some ten million three hundred thousand?

A. Ten million three hundred thousand, in that order.

Q. Am I to understand, then, that its use in this calculation here is to value the rate base or value those properties in the rate base that were acquired in 1956 at their purchase price value? That is its function or, you said, its effect?

A. Yes, plus the cost of any property acquired since that time.

Q. Right, but of course we have to take in additions and we take out retirements. But in regard to property that was acquired in 1956, the effect of your procedure here has been to reflect its current value based upon purchase price?

A. That is correct, yes, sir.

Q. It is a valuation device which you use?

A. That is right.

[Transcript pp. 779-781, cont.]

Q. May I ask, then, if the function of this is used as a valuation used to affect the purchase price values of property acquired in '56 which are still used and useful, why do you amortize this amount?

A. I amortize it because we are still depreciating the property on the basis of original cost. The effect of this depreciation on the basis of original cost amounts to something over two million dollars a year and we offset against that the amortization of this acquisition adjustment of one million dollars, so the net effect of it is to get down to depreciation on the basis of purchase price.

[Transcript pp. 809-810]

By Mr. Spiegel:

Q. You have said that this accrual of \$1,044,000 is really in the form of depreciation and could be accrued as an increase to the depreciation accrual on your operating statement. That is correct, that is what you said?

A. [Mr. Falk] I said normal cost of removal is provided as a part of depreciation, yes.

Q. So that this \$1,000,000, logically, could be combined with the depreciation figure of \$2,601,000?

A. We have not so treated it.

[Transcript pp. 809-810, cont.]

Q. But could logically be done that way?

A. I think it is being treated properly as it is to provide for it separately. Then we have it under control at all times for purposes of saying that it is used for track removal and any unused balance is disposed of at the direction of the Commission.

Q. In final analysis the justification for treating it as an operating expense is the same as the justification for treating depreciation accrual as an operating expense or operating deduction. The same logic applies to both of them.

A. I think it is a cost that has to be provided by the customers, yes.

[Transcript pp. 839]

By Mr. Goodman:

Q. Have you made any studies, Mr. Falk, concerning the adequacy or inadequacy of the provisions currently on the books for track removal, repaving and retirement of street car properties?

A. [Mr. Falk] I think I testified in my direct testimony that in my opinion we do not have enough experience yet to determine whether that provision is adequate or inadequate.

[Transcript pp. 839, cont.]

Q. Therefore the cost of track removal and re-paving, for example, may be more or less than the \$10,441,960 the company is presently allowed to accrue over the ten year period?

A. It may be more or less and it was so recognized by the Commission when we prescribed that amount, that it was purely an estimate and was subject to check as we get experience with actual track removal.

[Transcript pp. 918-919]

By Commissioner Kertz:

Q. I would like to ask Mr. Falk a question. Mr. Falk, some of the questions directed to you on cross examination relating to "financial cushions" seemed to me to indicate that in determining the revenue requirements of the company perhaps it would be inadvisable to have anything over and above the actual requirements, thereby eliminating the need for any cushion. You stated that you were providing a cushion, to some extent. In your opinion, does there exist a need for a cushion over and above the actual requirements as you compute them to be for the year 1960?

The Witness:

A. [Mr. Falk] With the situation with respect to Transit Company, you need something like that moreso

[Transcript pp. 918-919, cont.]

than you do with other companies. You don't have the growth -- at least, it is not anticipated that there will be growth to absorb increased costs. We do know that there are going to be increased costs beyond the costs that have been included in our future test period of the year 1960.

Commissioner Kertz: Would that include the present and anticipated future inflationary trends and costs of materials and supplies, for example?

The Witness: I think it is reasonable to assume -- I see no indication that costs are going to level off. We know that under the labor contract the company is going to incur increased labor costs during the next three years due to the life of the contract that they negotiated effective November 1, 1959.

[Transcript pp. 1086]

By Mr. Spear:

Q. Were you familiar with the terms of acquisition on August 15, 1956, of this company?

A. [Dr. Limmer] No.

Q. You haven't studied the original acquisition costs of this company or the terms of the contract of acquisition?

A. No; I haven't.



[Transcript pp. 1213]

By Mr. Spear:

Q. Have you ever tried to keep the books of any commercial concern, let alone utility, on a net of taxes basis on every entry? Have you ever tried to do it?

A. [Mr. Harris] No, sir, but in a case like this where it is an estimated future liability of no sum certain and it is not a deductible item on your tax claim, you do carry it as a net of tax --

[Transcript pp. 1218]

By Mr. Spear:

Q. Do you know any other utility that uses a net of tax theory for deductions which may not take place or even be considered for five years into the future? Do you know of any other utility, sir, that takes approach in any other accounting?

A. [Mr. Harris] No; I don't know of any specific instance. I am just advancing the logic of it and I still stand behind that.

[Transcript pp. 1301-02]

By Mr. Donnella:

Q. On Page 1042, Mr. Harris, you questioned the estimate of salvage made by Simpson and Curtin, the consultant engineers for the company, did you not?

[Transcript pp. 1301-02, cont.]

A. [Mr. Harris] Yes, sir.

Q. Do you consider the removal cost of only slightly more than one per cent of the estimated total is any real measure of the accuracy of the total estimate?

A. It is a very, very small sample, Mr. Donnella, but to the extent of the sample it does indicate salvage recovery of approximately 62 per cent of the total labor, materials and other costs involved in the track removal and repaving.

Q. Are you aware of the fact that a substantial amount of that salvage has been realized in connection with removing overhead copper trolley wire without any related cost for track removal?

A. No, sir; I am not aware.

[Transcript pp. 1497]

By Mr. Spear:

Q. Does it have any bearing on what the fares should be in the District of Columbia in this proceeding?

A. [Mr. Roberts] Not precisely, but it does indicate the median of the range of fares in these large cities and it can provide some guidance in determining reasonableness but not in determining a specific fare that will produce a fair return on the value of this property.

[Transcript pp. 1546-47]

By Mr. Spear:

Q. Now, sir, if the ten-million-three-hundred-thousand-dollar differential or excess, as it is called in the balance sheet, were, in fact, a measure and were, in fact descriptive of a liability assumed by the company to remove tracks and repave streets, and if it were so treated thereafter for both rate proceedings and such in this Commission, then, in fact, the purchase price of the assets would not have been or could not have been treated as the 13-1/2 million, but they would have had to be treated as the 23.8 million, would they not, if that assumption is correct?

A. [Mr. Falk] Well, no. I don't believe the purchase price would have been 13-1/2 million.

I do agree if that was considered as the liability then the portion of the purchase price that was related to the road and equipment would have been 17 or 18 million dollars instead of 7 or 8 million dollars, as has been worked out.

Q. Yes, or, to put it another way, if the company were not entitled to accrue a reserve for track-removal costs, and that is, if that track-removal cost were regarded as a liability assumed by the company when it acquired the assets, then correspondingly the base for both depreciation and

[Transcript pp. 1546-47, cont.]

system-rate base for rates would have had to include the additional amount of that obligation assumed under that interpretation at that time; correct?

A. Yes; I believe that is correct.

Certainly you would have been entitled to recover that amount through depreciation, and I think there would have been a good basis for claiming original cost on the rate base.

[Transcript pp. 1587]

By Mr. Bebachick:

Q. Mr. Falk, I believe you testified that the purchase price paid by the company reflected the liability assumed by the company for track removal and repaving.

A. [Mr. Falk] I said the purchase price reflected the liability?

Q. Yes.

A. No, sir.

I said that was an element that was considered, but I didn't say the purchase price reflected the cost of track removal. I said the fact that there was the liability for track removal was probably taken into consideration in arriving at the purchase price.

[Transcript pp. 1732-1735]

By Mr. Spear:

Q. Now, sir, would you describe what is shown by Exhibit 83 and how it was prepared?

A. [Mr. Curtin] This exhibit is designed to show what the impact of a five per cent increase in expenses would be in the City of Washington.

If we were to assume that the economic picture would be such here as to create a general five per cent increase in costs, it would affect everybody uniformly, the government, industrialists, the electric company, the gas company, the telephone company, the railroads, Greyhound and the D. C. Transit System.

What impact would it have upon their net income, the same five per cent, what impact would it have on their net income by reason of the operating ratios at which these utilities have functioned as indicated on the preceding exhibit?

What I have done is to take the operating ratio for each of these utilities for the last year reported, 1958, and carry them over to this Exhibit 83. The scale on the left indicates just the range of operating ratios and I have interpolated in there the particular figure applicable to each of the utilities listed in the year 1958.

[Transcript pp. 1732-1735, cont.]

The Potomac Electric Power Company had a 68 operating ratio in '58.

Chesapeake and Potomac had 74.76.

Washington Gas Light had 78.12, and so on.

Opposite each figure on the left there is a number indicating the per cent reduction in income that would result from a five per cent increase in operating costs. What impact would that have? Well, if you had a 50 per cent operating ratio, a five per cent increase in expenses would only make a five per cent bite in your net income. If you had a 70 per cent operating ratio it would make an 11 per cent bite into it. With an operating ratio of 80 per cent, it would bite off 20 per cent, the five per cent increase in expenses, of your net income, leaving 80 per cent still for the owners to plow back into the business.

You see, then, how as the operating ratio rises the margin left for the utility to absorb these changes narrows.

You see, also, what effect a five per cent change would have. It would cut the net income of Potomac Electric Power by 10.6 per cent, because it had an operating ratio of 68. The same change would cut Chesapeake' and Potomac Telephone's net income by nearly 15 per cent, 14.8, by reason of its 74.76. The Washington Gas Light, as a



[Transcript pp. 1732-1735, cont.]

result of a five per cent increase in expenses, would suffer an 18 per cent reduction in net. Greyhound, since it had an operating ratio up above 86, would lose nearly a third.

The railroads would lose, on a five per cent increase in expenses, 42 per cent of the remaining net income that they have.

D. C. Transit, with the same increase as all the others, would have its net income wiped out. One hundred per cent would be taken.

Q. What conclusion do you derive from the impact of a five per cent increase in expenses upon net income? What conclusion do you derive from that and from your prior exhibits?

A. Certainly it is not unreasonable to put any utility in a circumstance where it would be able to absorb a five per cent increase and still realize some respectable margin of profit. The figure which I have urged some 11 years ago and which has been substantially similar to the figure that the Congress found is applicable here is certainly in this scale reflected as being entirely reasonable.

An 86 operating ratio before taxes, or about 93 and a half after taxes, would put you in the same position as Greyhound Corporation.

[Transcript pp. 242]

By Mr. Donnella:

Q. Is there any particular reason why they are deposited outside the District of Columbia, Mr. Flanagan?

A. [Mr. Flanagan] Only Mr. Chalk could answer that. I am in no position to answer that, Mr. Donnella.

Q. You don't know?

A. I don't know.

Q. Do you know whether or not any of those cash funds are pledged or encumbered in any way?

A. I am sure they are not.

Q. They are not?

A. No, sir.

[Transcript pp. 1848-49]

By Mr. Goodman:

Q. When you were Chairman of the Commission, this Commission, Capital Transit in each rate case computed a cost of capital figure, did it not, taking a certain per cent on equity and a certain per cent for debt, to obtain a fair return allowance?

A. [Mr. Flanagan] We had many rate cases with both Capital Transit and other utilities and I am sure in some of them, at least, testimony was taken as to the cost of capital.

[Transcript pp. 1848-49, cont.]

Q. Was this the method that the Commission used in each of the rate cases, beginning with the one in 1945?

A. I don't recall that it was used in each case. As a matter of fact, just because testimony was presented in the record would not be indicative that that was the basis upon which the Commission made its determination.

Q. And in computing the cost of equity the company often relied upon earnings price ratio studies, did it not?

A. Not on earnings price ratios of transit companies, never to my knowledge. They are entirely and completely unreliable and always have been.

D. C. TRANSIT SYSTEM, INC.  
 Estimated Rate of Return to be Earned  
 under the proposed D. C. Fare Structure of  
 25¢ Cash; Tokens 5 for \$1.00; 10¢ School Fare

1. Estimated increase in gross revenues resulting from proposed D. C. fare structure		\$ 1,305,810
2. Adjusted to System-wide basis (Line 1 + 93.50%)		\$ 1,396,588
3. Adjusted for estimated portion of year 1960 that proposed increased fares will be in effect (10/12ths of Line 2)		\$ 1,163,823
4. Increase in Net Operating Income after adjustment for the effect of income tax and injuries and damages accruals (Line 3 x 41.51%)		\$ 483,103
5. Net Operating Income at present fares (Exh. No. ____, Schedule 1)		\$ 660,146
6. Increase in Net Operating Income, above		<u>483,103</u>
7. Net Operating Income at proposed fares		<u>\$ 1,143,249</u>
8. Average investment in Rate Base Property (Exh. No. ____, Schedule ____)		<u>\$16,016,810</u>
9. Adjusted Gross Operating Revenues:		
At present fares	\$26,708,655	
Estimated increase from proposed fares	<u>1,163,823</u>	<u>\$27,872,478</u>
10. Rate of Return Earned on:		
Investment in Rate Base Property (Line 7 + Line 8)		7.14%
Gross Operating Revenues (Line 7 + Line 9)		4.10%

D.C. TRANSIT SYSTEM, INC.

ESTIMATED INCREASE IN DISTRICT OF COLUMBIA PASSENGER REVENUE IN 1960 ANNUAL PERIOD  
BY INCREASING ADULT FARES FROM PRESENT 20 CENTS TO 25 CENTS CASH, 5 TOKENS FOR \$1 AT ALL HOURS

	At Present Fares Passenger Revenue (1)	Passenger Revenue (2)	Present Fare (3)	Proposed Fare (4)	Per Cent Increase in Fare (5)	Passengers Paying Proposed Fare Per Cent (6)	Number (7)	Estimated Passenger Revenue at Proposed Fares (8)	Estimated Increase in Passenger Revenue (9)	Per Cent Increase in Revenue from Pro- posed Fares (10)
Prospective Cash Passengers	\$ 7,597,442	37,987,209	20	25	25 %	93.75 %	35,613,009	\$ 8,903,252	\$1,305,810	
Prospective Token Passengers	<u>16,619,404</u>	<u>83,097,023</u>	20	20	0	100.00	<u>83,097,023</u>	<u>16,619,404</u>	<u>-</u>	
Total Adults	\$24,216,846	121,084,232	20	21.50	7.50	98.04	118,710,032	\$25,522,656	\$1,305,810	
Students	<u>505,137</u>	<u>5,051,371</u>	10	10	0	100.00	<u>5,051,371</u>	<u>505,137</u>	<u>-</u>	
All Passengers	\$24,721,983	126,135,603	19.60	21.03	7.30	98.12	123,761,403	\$26,027,793	\$1,305,810	5.25 %

It is assumed in the above computation that 70% of the adult passengers will use the 20-cent tokens and 30% will pay the 25-cent cash fare. It is further assumed that of those passengers affected by the 25% increase in the cash fare, 64% of such passengers will withdraw their patronage rather than pay the 25-cent fare.

REPLY BRIEF OF APPELLANTS

---

**United States Court of Appeals**

FOR THE DISTRICT OF COLUMBIA CIRCUIT

---

No. 16,454

---

LEONARD N. BEBCHICK, AND  
LEONARD S. GOODMAN

APPELLANTS

VS.

PUBLIC UTILITIES COMMISSION OF  
THE DISTRICT OF COLUMBIA, AND  
D. C. TRANSIT SYSTEM, INC.

APPELLEES

---

APPEAL FROM AN ORDER OF THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

---

OF COUNSEL

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United States Court of Appeals  
for the District of Columbia Circuit

DEC 18 1961

*Joseph H. O'Brien*

CLERK

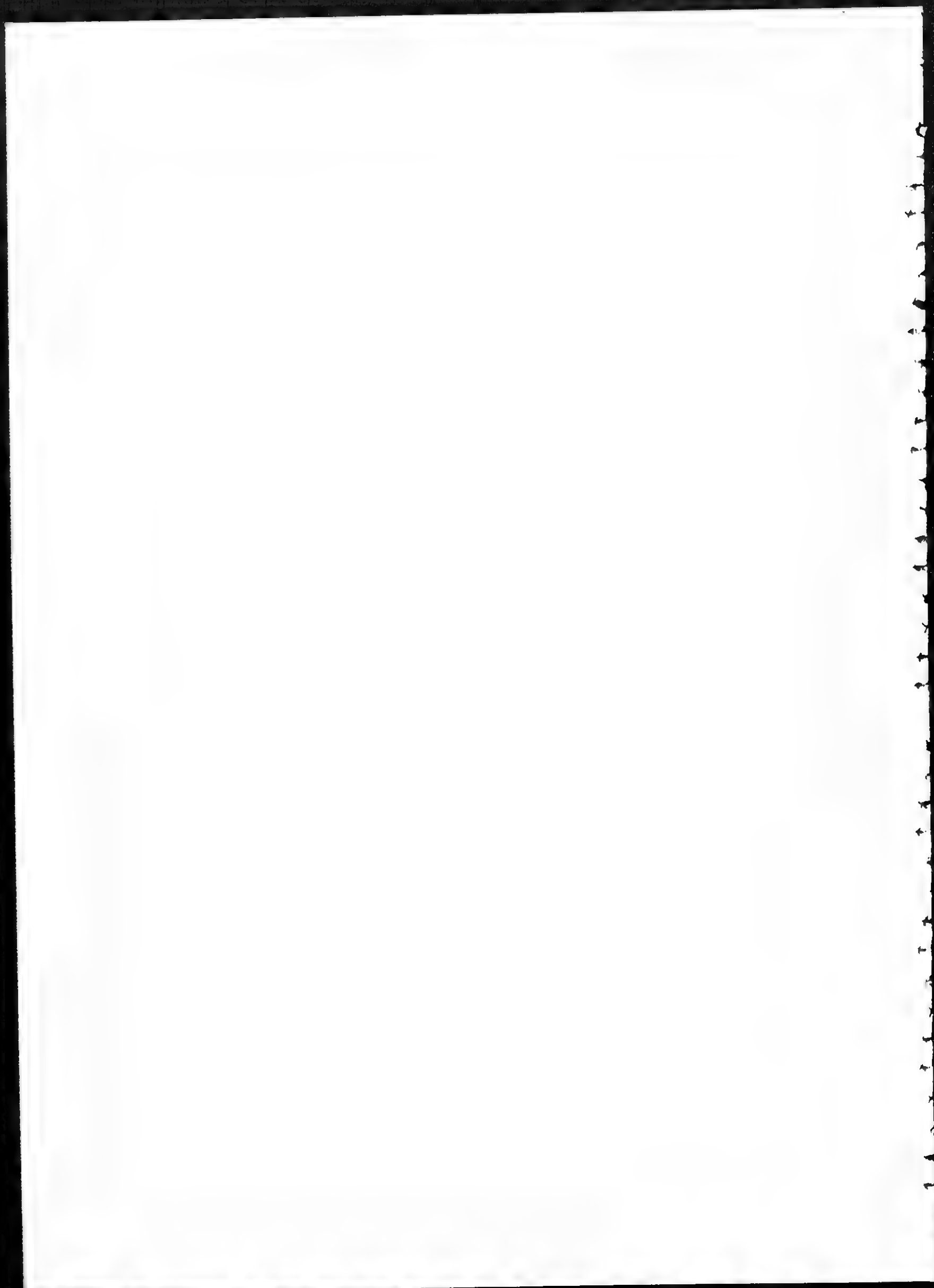
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**UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT**

---

**No. 16,454**

---

**Leonard N. Bebhick, and  
Leonard S. Goodman**

**Appellants**

**vs.**

**Public Utilities Commission of  
the District of Columbia, and  
D. C. Transit System, Inc.**

**Appellees**

**APPEAL FROM AN ORDER OF THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT OF COLUMBIA**

SUBJECT INDEX

ARGUMENT . . . . .	1
I. THIS APPEAL AND THE ISSUES PRESENTED ARE NOT MOOT . . . . .	1
II. AN ORDER OR RESTITUTION IS AVAILABLE IN THIS PROCEEDING . . . . .	5
III. THE FRANCHISE DOES NOT ENTITLE TRANSIT TO A SPECIFIC RATE OF RETURN . . . . .	8
APPENDIX A . . . . .	A-1

# CASES CITED

<u>Arkadelphia Milling Co. v. St. Louis S.W. Ry. Co.</u> , 249 U.S. 134, 145 (1919) . . . . .	6
<u>Atlantic Coast Line R.R. v. Florida</u> , 295 U.S. 301 (1935) . . . . .	6
<u>Baltimore &amp; Ohio Ry. Co. v. United States</u> , 279 U.S. 781, 786 (1928) . . . . .	6
<u>*Capital Transit Co. v. Public Utilities Commission</u> , 93 U.S. App. D.C. 194, 213-215, 213 F2d 176, 194-196 (1953) <u>cert. denied</u> , 348 U.S. 816 (1954) . . . . .	6
<u>*Eastern Airlines v. Civil Aeronautics Board</u> , 87 U.S. App. 331, 185 F2d 426 (1950) . . . . .	4
<u>Ex Parte Lincoln Gas Co.</u> , 256 U.S. 512, 516-517 (1921) . . . . .	7
<u>Ford Motor Co. v. United States</u> , 335 U.S. 303, 313 (1948) . . . . .	4
<u>*Gay Union Corporation v. Wallace</u> , 71 U.S. App. D.C. 382, 112 F2d 192 (1940) <u>cert. denied</u> , 310 U.S. 647 (1940) . . . . .	4
<u>Mitchell v. Riegel Textile, Inc.</u> , 259 F2d 954 (CA DC, 1958) . . . . .	6
<u>Southern Pacific Co. v. Interstate Commerce Commission</u> , 219 U.S. 433, 452 (1911) . . . . .	4
<u>Southern Pacific Terminal Co. v. Interstate Commerce Commission</u> , 219 U.S. 498, 515 (1911) . . . . .	3
<u>United Gas Co. v. Mobile Gas Corp.</u> , 350 U.S. 332, 347 (1956) . . . . .	6
<u>Virginia Petroleum Jobbers Assn. v. FPC</u> 104 App. D.C. 106, 259 F2d 921 (1958) . . . . .	8

* <u>Washington Gas Light Co. v. Baker,</u> 88 U.S. App. D.C. 115, 188 F2d 11, 23 (1950), <u>cert. denied,</u> 340 U.S. 952 (1951) . . . . .	8
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\*Cases chiefly relied upon are marked  
by asterisks.

#### STATUTES CITED

Act of March 4, 1913, 37 Stat. 989, ch. 150, § 8, par. 69, as amended August 27, 1935, 49 Stat. 884, ch. 742, §2, District of Columbia Code, 1961, Title 43, Section 709 . . . . .	1
Act of July 24, 1956, 70 Stat. 598 (the "Franchise") . . . . .	12
Section 4 . . . . .	9-12
Section 9 . . . . .	11
Act of September 15, 1960, 74 Stat. 1031, Title II (the "Compact") . . . . .	12
Section 21 . . . . .	3
Section 23(a) . . . . .	3

#### MISCELLANEOUS

House Report 1621, 86th Congress, 2nd Session. . . . .	12
1 Moore's Federal Practice 4022-23 (2d ed., 1960) . . . . .	9

## ARGUMENT

### I

#### THIS APPEAL AND THE ISSUES PRESENTED ARE NOT MOOT

There is no merit to appellees' afterthought that this appeal is moot because, pending appeal of the Order under review, the Commission promulgated Order 4735 regarding the rates charged by Transit.

1. Appellees' contention is clearly unsound. Otherwise the Commission could perpetually avoid judicial review by initiating proceedings regarding outstanding rates and entering new orders just prior to the hearing of the appeal. This is not good sense and it is not good law. The suggestion has been rejected by this Court. And Congress has specifically blocked any such maneuver.

2. If the Commission's Order 4735 had superseded the Order 4631 (here under review) that would not have mooted any judicial appeal. For Title 43, §709, of the District of Columbia Code<sup>1/</sup> specifically provides that once a Commission order has been appealed an amendatory order of the Commission shall not moot the appeal but merely take the place of the order under

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<sup>1/</sup> "The Commission may at any time, rescind, alter, modify, or amend its order. If, after appeal is filed, the Commission shall rescind the order or decision appealed from, the appeal shall be dismissed; if it shall alter, modify, or amend the same, such altered, modified, or amended order or decision shall take the place of the original order and the court shall proceed thereon as though the late order had been made by the Commission in the first instance. "



appeal. Under the Statute, an appeal is mooted only when the Order appealed from is rescinded by the Commission.<sup>2/</sup>

3. However, it is plain on the very face of Order 4735 (Appendix infra, p. A-3.), that it was not intended to, and did not rescind, supersede or affect the vitality of Order 4631.<sup>3/</sup> On the contrary the Commission expressly declined to interfere with the mandate of Order 4631. Its order specifically provided (§2) "that the present schedule of rates . . . shall remain in effect." The scope of Transit's obligation to "conform" to outstanding orders of the Commission (43 D.C. Code 701) was left unchanged. Transit was not required to and it did not make any "changes in their schedule on file."

4. The Commission's findings and conclusions of reasonableness embodied in Order 4735, and Opinion in Support, rest upon the same principles and approach as its Order 4631 -- principles which appellants challenge as erroneous.

The Commission continued to allow Transit to accrue over \$1 million per annum for track removal and repaving in the absence of any evidence of any immediate need for such accruals; to allow depreciation and amortization of abandoned

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<sup>2/</sup> If appellees seriously considered that Order 4735 superseded Order 4631 they would have raised this contention in the District Court which could then have effectuated 43 D.C. Code 709 by consolidating this case with the appeal then on file from Order 4735 (C.A. 825-61).

<sup>3/</sup> In initiating its investigation which culminated in Order 4731, the Commission established the scope of the investigation as the reasonableness of the increased fares proposed by Transit (Appendix A-1).

streetcar properties; to allow depreciation for fully-depreciated buses (in regard to the first 6 months of the base period); to fix a rate base substantially beyond the prudent investment; to include abandoned properties and operating reserves in the rate base, etc.

These questions will continue to recur regardless of the administrative forum in which Transit will seek to obtain fare increases. Title II, Section 21, of the Compact (74 Stat. 1031) continues in effect all lawful orders of the appellee Commission, and will continue in effect the errors of the present order and decisions unless set aside by this Court.<sup>4/</sup>

5. Even where an administrative determination is no longer in effect, the Court will consider its validity where the appeal presents important questions likely to recur.

In passing upon the legality of a short-term ICC order which enjoined an undue preference and which had expired prior to a final judicial hearing, the Supreme Court noted, Southern Pacific Terminal Co. v. Interstate Commerce Commission, 219 U.S. 498, 515 (1911):

"In the case at bar the order of the Commission may to some extent (the exact extent it is unnecessary to define) be the basis of further proceedings. But there is

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<sup>4/</sup> This suit filed prior to the enactment of the Compact is specifically saved by Title II, Section 23(a) of the Compact.

a broader consideration. The questions involved in the orders of the Interstate Commerce Commission are usually continuing (as are manifestly those in the case at bar) and their consideration ought not to be, as they might be, defeated, by short term orders, capable of repetition, yet evading review, and at one time the Government and at another time the carriers have their rights determined by the Commission without a chance of redress."

See also Southern Pacific Co. v. Interstate Commerce Commission, 219 U.S. 433, 452 (1911); Ford Motor Co. v. United States, 335 U.S. 303, 313 (1948).

In Gay Union Corporation v. Wallace, 71 U.S. APP. D.C. 382, 112 F2d 192 (1940) cert. den., 310 US 647 (1940), this Court reviewed the legality of acreage controls no longer in effect due to the abandonment of the control program. The Court noted that the Secretary of Agriculture had recently promulgated regulations which created the possibility of the issuance of substantially similar acreage allotments in the future and accordingly proceeded to the merits.

In Eastern Airlines v. Civil Aeronautics Board, 87 US APP. D. C. 331, 185 F2d 426 (1950), this Court considered the legality of the use by the CAB of its exemption authority, although the specific exemption order being challenged had expired. The possibility of the future issuance of similar orders raising similar questions of law led the Court to retain jurisdiction. The Court felt that the appeal presented an important recurring question.

The authorities relied upon by appellees are readily distinguished. They do not deal with situations where the clear possibility exists of future administrative action of substantially similar nature giving rise to substantially similar issues of law.

6. Finally, appellants can obtain a vital portion of the relief they request -- the funding of monies collected by Transit under an unlawful fare -- only by a decision on this case. This point is considered at length in the following section.

## II

### AN ORDER OF RESTITUTION IS AVAILABLE IN THIS PROCEEDING

Appellants specifically request that this Court award such relief as will require Transit to fund and account for all revenues which it has received as a result of the increase in its cash fare from 20 to 25 cents since the effective date of the increase, March 6, 1960.

Transit asserts that such a remedy is beyond the power of the courts and relies upon obscure and irrelevant precedent. Transit pointedly fails to recognize that such restitution is well established, and that this Court in respect to this Commission awarded precisely such relief in favor of Transit's predecessor Company.

In Capital Transit Co. v. Public Utilities Commission 93 U.S. App. D.C. 194, 213-215, 213 F2d 176, 194-196 (1953), cert. denied, 348 US 816 (1954), this Court reversed a rate order of appellee Commission which permitted the Potomac Electric Power & Light Company (PEPCO) to increase its rates. This Court directed the District Court to order PEPCO to segregate all amounts collected from appellant Capital Transit Company, one of its customers, by reason of the rate increases. The disposition of such proceeds was left for further determination. In awarding such relief, the Court set forth the considerable precedent for such relief in the nature of restitution, and appellants rely thereon, and the authorities cited. Judge Stephens questioned the authority of this Court to directly order such relief. However, all members of the panel joined in support of the principle of restitution. See also Mitchell v. Riegel Textile, Inc., 259 F2d 954 (CA DC, 1958).

The position taken by this Court is clearly supported by precedent. Baltimore & Ohio Ry. Co. v. United States, 279 US 781, 786 (1928). See also Arkadelphia Milling Co. v. St. Louis S.W. Ry. Co., 249 US 134, 145 (1919) and United Gas Co. v. Mobile Gas Corp., 350 US 332, 347 (1956).

Appellees cite Atlantic Coast Line R.R. v. Florida, 295 U.S. 301 (1935). That case plainly approves the general



doctrine of restitution. It carved out an exception on particular facts that have no application to the case at bar.<sup>5/</sup>

Restitution of revenues collected under an unlawful order may be awarded not only in suits by an injured individual but also in a suit by a representative of a class of consumers. The Supreme Court has held that it is a utilities equitable duty to refund excess charges to the consumers and that this duty was enforceable even where the consumers were not parties to the litigation since the nominal parties "were, in a broad sense, the representatives of the consumers, the parties actually concerned", and since the customers were "so many in number, and the difficulty of sustaining their individual claims through separate suits would be so great, that to remit them to such suits would be a virtual denial to justice."

Ex parte Lincoln Gas Co. 256 US 512, 516-517 (1921). And this Court has said that parties aggrieved by an administrative

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<sup>5/</sup> The Supreme Court, while recognizing this rule of restitution "as one of general application", held that "exceptions" were called for where in the peculiar facts of the particular case, the ICC's order was rendered voidable by the absence of technical findings required when the ICC prescribed intrastate rates, although its findings were supported by the evidence. The Court also relied upon the fact, in refusing to sanction restitution, that the ICC itself did not have jurisdiction to award reparation for unreasonably high intrastate rates (295 US at 311), it being a Federal agency with primary authority in interstate commerce and only incidental "Shreveport" authority in intrastate commerce. Of course, it is clear the rule of "general application" applies in the present case, rather than the "exception" of the Coast Line case.



agency order in their nature "act as representatives of the public interest in seeking judicial review. Virginia Petroleum Jobbers Assn. v. FPC, 104 App D.C. 106, 259 F2d 921 (1958). The principle of awarding restitution to benefit consumers in a suit brought by an individual consumer has been recognized by this Court. Washington Gas Light Co. v. Baker 88 U.S. App. D.C. 115, 138 F2d 11, 23 (1950), cert. denied, 340 U.S. 952 (1951).

### III

#### THE FRANCHISE DOES NOT ENTITLE TRANSIT TO A SPECIFIC RATE OF RETURN

Transit argues that its Franchise expresses a Congressional mandate that a return of 6-1/2 per centum on either the rate base or gross operating revenues (depending upon the standard employed by the Commission) is reasonable. It concludes that a fortiori a return of 4.1% on gross operating revenues is reasonable as a matter of law.<sup>6/</sup>

1. Transit took a separate appeal from the Commission's Order (No. 4631), because the Commission rejected an "alternative" fare proposal of 5 tokens for \$1.10 that Transit contended had been introduced at hearing. (C.A. 1439-60).

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<sup>6/</sup> Under the fare increase approved by the Commission, Transit earns a return in excess of 6-1/2% on the system rate base.

Transit contended that it was entitled as a matter of law to earn 6-1/2% on operating revenues. Transit asserted and the Commission conceded that the return from its proposal would be less than 6-1/2% of operating revenues. Transit inserted an identical claim in this case before the District Court by means of a cross-claim (inaccurately denominated a counterclaim) against the Commission. This cross-claim was subsequently dismissed by stipulation.

On Transit's appeal, Transit's contention was rejected by the District Court and judgment was granted in favor of the Commission. Transit appealed to this Court. (No. 16,107)<sup>7/</sup> A few days prior to the scheduled argument, Transit and the Commission stipulated to a dismissal of the appeal, allowing the decision of the District Court to govern on this question of law. The parties are accordingly collaterally estopped as to such matters in this litigation. 1 Moore's Federal Practice 4022-23 (2d ed., 1960).

2. The Commission argued in its Brief filed in this Court in No. 16,107 that the governing standard of the Franchise was "the requirements of Section 4 that the return should be at a level to make the Corporation an attractive investment for private enterprise." Commission's brief in No. 16,107, p. 17. The Commission continued:

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<sup>7/</sup> These appellants were permitted to file a brief as amicus curiae.

"It is inconceivable that Congress intended, when it stated in Section 4 that the Company should be entitled to a return in accordance with standards and rules prescribed by this Commission, that the Commission would be required to accept rates filed by the Company that would produce the level of earnings heretofore referred to [i.e., 6-1/2 percent] without any discretion on the part of the Commission as to whether or not such rates represented a proper balancing of investor and customer interests." 8/

The District Court correctly found that the reference to 6-1/2% in the Franchise does not foreclose the Commission from exercising its administrative discretion as to the reasonableness of any fare structure yielding less than 6-1/2%. If the Commission has discretion to determine fares yielding less than 6-1/2%, the exercise of this discretion is reviewable. 9/

3. Congress stated in the second sentence of Section 4 of the Franchise that "as an incident" to making Transit an attractive investment a return of at least 6.5 percent would

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8/ Similarly the Commission's opposition in the District Court to Transit's motion for summary judgment stated (p. 6): "The Commission is not required, as a matter of law, to authorize a particular fare structure which the Company proposes that would yield less than 6-1/2% on its gross operating revenue."

9/ Of course, appellees' present construction of the legislative reference to a 6-1/2 percent rate of return is at best only a partial defense to the issues raised on this appeal. The legality of numerous Commission actions remain for decision. Indeed, if the Court should agree with appellants that any number of the revenue deductions which the Commission allowed are improper, Transit would realize a return of 6-1/2 percent of its gross operating revenues—even under a 20 cent cash fare.

not be unreasonable. The specific return figure applies only "as an incident" to enable the company to attract capital, and hence if 6.5 percent, or more, is not so needed, the legislative "finding" does not apply.

The reference to 6-1/2% in Section 9 was a guarantee to the Company in a limited sense, -- that if the fares prescribed by the Commission yielded less than 6-1/2%, the Company would have the assurance of the subsidy.

The reference to 6-1/2% in Section 4 served to harmonize §4 with §9.

If there had been no reference to 6-1/2% in Section 4, a consumer might well have contended that the Commission had no discretion to prescribe rates on the basis of a 6-1/2% return, and that Congress intended that the rates paid by the consumers should yield something less than 6-1/2%, with the subsidy (under §9) provided by the taxpayers making up the difference.

By including the reference to 6-1/2% in Section 4 Congress negatived any such arguments and made it clear that the Commission could (and should) prescribe a 6-1/2% rate -- throwing the full burden on the consumers -- if this was the appropriate rate under established principles of public utility regulation, i.e., the rate required to attract private capital.

In other words Congress did not intend to burden the taxpayers if the consumers could properly be required to provide a 6-1/2% return through fares.

4. In enacting the Compact, Congress in turn merely pointed to what had been stated in the Franchise regarding rate of return, and that it sought to "preserve those provisions". House Report 1621, 86th Congress, 2d Session, p. 26.

The Commission, in construing Transit's Franchise over a four-year period consistently acted upon the express belief that it possessed statutory authority to determine a reasonable rate of return for Transit, the reference to 6-1/2% notwithstanding. In passing the Compact and establishing a successor regulatory agency Congress adopted the language of the Franchise without any adverse reference at any stage of the legislative process to this interpretation of the Commission. The inevitable conclusion is that the Commission's interpretation correctly reflected the original intent of Congress; this Congressional repetition of substantially the same language is a reenactment confirming the adoption of the Commission's interpretation of the meaning

of the 6-1/2 % reference in Section 4 of the Franchise.

Respectfully submitted

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Attorneys for Appellants

December 18, 1961



APPENDIX

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

Order No. 4694

September 15, 1960

IN THE MATTER OF	)	
	)	P.U.C. No. 3640
Change in Schedule of Rates of	)	Formal Case No. 474
D. C. TRANSIT SYSTEM, INC.	)	

ORDER OF SUSPENSION AND NOTICE OF HEARING

D. C. Transit System, Inc. filed with the Commission on September 14, 1960, notice that the following schedule of rates will be adopted by the Company, effective November 1, 1960:

Cash Fare	\$ .25
Token Fare	To be sold in units of 4 for \$.95
School Fare	\$.10, with tickets to be sold in units of 10 for \$1.00 or 20 for \$2.00.

Upon consideration of the notice of the Company of its intention to adopt the schedule of rates as set forth above,

IT IS ORDERED:

Section 1. That, pursuant to Section 5 of Public Law 757, 84th Congress, 2nd Session, the schedule of Proposed rates filed by D. C. Transit System, Inc., on September 14, 1960, to become effective on November 1, 1960, be, and it is hereby suspended for a period of 120 days from the date of filing, unless otherwise ordered by the Commission.

Section 2. That an investigation be made of the reasonableness of the rate schedule filed.

Pursuant thereto, notice is hereby given that a formal public hearing will be held in Room 500, District Building, at 10:00 a.m., on Monday, September 29, 1960, at which time

Page 2, Order No. 4694

D. C. Transit System, Inc. shall make available a competent witness or witnesses for examination on all material and relevant facts and be prepared to present all pertinent data in support of its proposed new schedule of rates.

A TRUE COPY:

By the Commission:

Chief Clerk

Sarah E. Wilson  
Acting Executive Secretary

mfs

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

Order No. 4735

January 18, 1961

IN THE MATTER OF

Petition of D. C. TRANSIT SYSTEM, INC.)  
For Change in Schedule of Rates. )

P.U.C. No. 3640

Formal Case No. 474

\* \* \*

Findings and Conclusions

Upon consideration of the entire record in this proceeding, which will be discussed in detail in the supporting opinion hereafter to be filed, the Commission finds and concludes:

1. That the gross operating revenue method should be utilized for measuring rate of return in this proceeding.

2. That the system rate base applicable to mass transportation operations provides a useful means to check the reasonableness of the result obtained from the use of the gross operating revenue method and should be utilized.

3. That the proper past test period for measuring the actual level of earnings, under the circumstances in this case, is the six months ended August 31, 1960.

4. That the proper test period for measuring estimated level of future earnings, under the circumstances in this case, is the twelve months ending February 28, 1961.

5. That depreciation on buses should be based upon the actual experience of the Company, where available, rather than upon theoretical studies or purported comparable situations.

6. That based upon the actual experience of this Company the average service life of its buses is 17 years.

7. That the straight line method of accruing depreciation adopted by this Commission in prior proceedings is appropriate for use in this proceeding and should be used.

Order No. 4735

8. That the record demonstrates that the group method of depreciation is not the most desirable method for depreciating buses.

9. That the unit method of depreciation should be utilized by this Company for its buses and that a single purchase of like buses may be treated as a unit.

10. That the annual rate of depreciation applicable to buses, including spare parts and accessories, should be 5.74 per cent, which is equivalent to a 17-year life with 2.5 per cent salvage.

11. That the present annual rate of depreciation on buses, spare parts and accessories of 7 per cent be terminated as of August 31, 1960, and thereafter the annual rate of depreciation on said items shall be 5.74 per cent.

12. That the present fleet of 1,060 buses contains 366 buses that have been fully depreciated as of August 31, 1960, of which latter number 336 buses are over 18 years of age.

13. That the group method of depreciation for buses, heretofore used, has resulted in an excess accrual of depreciation, based upon the investment in the 1,060 buses still in service, in the amount of \$2,414,638.

14. That the excess depreciation accrued on buses in the amount of \$2,414,638 will be more than sufficient to meet anticipated retirement losses on the remaining rail facilities and should be used for this purpose, with the remainder to be applied, if needed, to other property.

15. The excess depreciation accrual of \$2,414,638, arising from bus property, will eliminate any present need to increase the annual rates of depreciation on other than bus property.

16. That original cost less estimated salvage is an appropriate base for measurement of depreciation expense, is just and equitable for both investors and rate payers, and should be used.

17. That the use of reproduction cost or other conjectural value is not an appropriate base for the measurement of depreciation expense in this proceeding.

18. That the net operating income from system-wide mass transportation operations at present fares for the twelve

months ending February 28, 1961 is estimated to be \$1,398,800 after giving effect to appropriate adjustment for depreciation on buses, heretofore determined to be proper.

19. That gross operating revenue from system-wide mass transportation operations at present fares for the twelve months ending February 28, 1961 is estimated to be \$28,412,526.

20. That estimated net operating income of \$1,398,800 for the twelve months ending February 28, 1961 will produce a rate of return of 4.92 per cent, on estimated gross operating revenues of \$28,412,528.

21. That the mass transportation system rate base for the twelve months ending February 28, 1961 is \$16,821,310, which amount is proper for measuring the reasonableness of the return earned thereon.

22. That the estimated net operating income of \$1,398,800 for the twelve months ending February 28, 1961 will produce a rate of return of 8.31 per cent on the rate base of \$16,821,310.

23. That earnings of \$1,398,800, equivalent to a rate of return of either 4.92 per cent on gross operating revenues or 8.31 per cent on rate base, fall within the range of what we consider to be a fair return and will provide sufficient revenue to meet all allowable expenses, including taxes and depreciation, interest on debt, plus reasonable dividends and an increment for surplus commensurate with the risk involved.

24. That the earnings-price ratio method of determining allowable return on equity is not an appropriate method to be used in this proceeding.

25. That there is nothing in the record to justify changing the amount of \$10,441,958, heretofore found by this Commission to be a reasonable estimate of the total costs for track removal and repaving.

26. That the ten-year period from August 1956, heretofore determined by this Commission for accruing the estimated track removal and repaving costs of \$10,441,958, is reasonable.

27. That the application of the Company to change its present District of Columbia Schedule of Rates from a 25-cent cash fare, tokens at 5 for \$1.00, and a 10-cent school fare to a 25-cent cash fare, tokens at 4 for \$.95, and a 10-cent school fare, has not been satisfactorily supported, has not been shown to be in the public interest, is not warranted, and is accordingly denied.



28. That the present District of Columbia Schedule of Rates consisting of a 25-cent cash fare, tokens at 5 for \$1.00, and a 10-cent school fare is just, reasonable, and compensatory and will enable the Company to meet its obligations, to maintain a sound financial structure, to reasonably compensate investors, and to furnish service adequate to meet the growing needs of the community.

NOW, THEREFORE, IT IS ORDERED:

Section 1. That the petition of D. C. Transit System, Inc. for a change in its schedule of rates applicable to the District of Columbia for a cash fare of 25¢, token fare of 4 tokens for 95¢, and a school fare of 10¢ with tickets to be sold in units of 10 for \$1.00 or 20 for \$2.00, which schedule was to become effective November 1, 1960, and was suspended for a period of 120 days from the date of filing by Order No. 4694, dated September 15, 1960, is denied.

Section 2. That the present schedule of rates applicable to the District of Columbia, consisting of a cash fare of 25¢, token fare of 5 tokens for \$1.00, and a 10¢ school fare, is just, reasonable, and nondiscriminatory and shall remain in effect.

Section 3. That the annual rate of depreciation heretofore applicable to buses, including spare parts and accessories, of 7 per cent shall be terminated as of August 31, 1960.

Section 4. That on and after September 1, 1960, the annual rate of depreciation applicable to buses, including spare parts and accessories, shall be 5.74 per cent.

Section 5. That the group method of depreciation heretofore applicable to buses, including spare parts and accessories, shall be terminated as of August 31, 1960.

Section 6. That on and after September 1, 1960, the unit method of depreciation applicable to buses, including spare parts and accessories, shall be utilized.

Section 7. That the Company shall make appropriate adjustments on its books to reflect the changes in rate and method of depreciation applicable to buses, including spare parts and accessories, herein presented.

A TRUE COPY:

By the Commission:

Chief Clerk.

Norman B. Belt  
Executive Secretary



J O I N T   A P P E N D I X

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

LEONARD N. BEBCHICK, AND  
LEONARD S. GOODMAN

APPELLANTS

VS.

PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA,  
AND D.C. TRANSIT SYSTEM, INC.

APPELLEES

NO. 16,454

APPEAL FROM AN ORDER OF  
THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA

United States Court of Appeals  
for the District of Columbia Circuit

OCT 4 1961

*Joseph B. Sisk*

CLERK

TABLE OF CONTENTS

	<u>Page</u>
PUC Order No. 4631 of March 2, 1960 -- Excerpts . . . . .	1
PUC Opinion in Support of Order No. 4631 of March 31, 1960 -- Excerpts . . . . .	5
Complaint . . . . .	32
Order of the District Court . . . . .	39
Notice of Appeal . . . . .	42
Exhibits Admitted in Commission Hearing:	
<u>No.</u>	
4 . . . . .	43
5 . . . . .	44
6 . . . . .	46
7 . . . . .	47
10-A (last page) . . . . .	48
16 . . . . .	49
30 . . . . .	50
39 (page 1, sched. 3 & sched. 4) . . . . .	51
42 (page 2) . . . . .	55
43 . . . . .	57
46 . . . . .	61
48 (page 1) . . . . .	63
49 . . . . .	65
50 . . . . .	66
51-A . . . . .	67
53 . . . . .	69
54-A . . . . .	70
59 . . . . .	73

TABLE OF CONTENTS  
(Continued)

<u>No.</u>	<u>Page</u>
88 . . . . .	75
91 (pages 1, 3-8, Exhibits 2 & 4) . . . . .	80
Excerpts from Transcript of Commission Hearing (listed in numerical page progression) . . . . .	89
Supplemental designation (pages 824-25, 928-930 865-868) . . . . .	255

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

Order No. 4631

March 2, 1960

IN THE MATTER OF

Petition of D. C. TRANSIT SYSTEM, INC.  
For Change in Schedule of Rates.

} P.U.C. No. 3628  
Formal Case No. 471

\* \* \*

Findings, Conclusions, and Order

\* \* \*

Findings

Upon consideration of the record in this proceeding which will be discussed in full detail in the supporting opinion hereafter to be filed, the Commission finds:

1. That the Company has complied substantially with the intent of the Franchise Act and with the conditions heretofore indicated by the Commission as warranting the utilization of the gross operating revenue method for rate-making purposes in keeping with the legislative policy declared in Section 4 of the Act.
2. That the twelve months ended September 30, 1959, is a proper period for determining the Company's actual level of earnings for a past test period.
3. That the twelve months ending December 31, 1960, is a proper period for measuring the Company's estimated level of earnings for a future test period, after giving effect to appropriate adjustments for changes in the level of revenues and expenses.
4. That the estimates of operating results for the years 1961 and 1962 are not sufficiently reliable to serve as a basis for providing, at this time, for an increase in rates to become effective on November 1, 1960, as proposed by the Company.
5. That net operating income from system-wide mass transportation operations for the future test period ending December 31, 1960, is estimated to be \$660,146.

6. That system operating revenues applicable to mass transportation operations for the future test period, at present rates, are estimated to be \$26,708,655.

7. That the system rate base applicable to mass transportation operations, for the future test period, determined by giving equal weight to net original cost and to purchase price of the property is \$16,016,810.

8. That net operating income of \$660,146 for the future test period will provide the Company with a return of 2.47% on gross operating revenues of \$26,708,655 and a return of 4.12% on the rate base of \$16,016,810.

9. That the District of Columbia fare structure originally proposed by the Company of a 25 cent cash fare during weekday rush hours, a 20 cent cash fare during all other periods, and a 10 cent school fare would provide the Company with a return of 5.58% on adjusted gross operating revenues of \$29,015,408 for the future test period, and a return of 10.10% on the rate base of \$16,016,810.

10. That the District of Columbia fare structure proposed by the staff of the Commission of a 25 cent cash fare, tokens at 5 for \$1.00, and a 10 cent school fare, together with a comparable increase in fares from the Company's other mass transportation operations, will produce net operating income on a system-wide basis for the future test period, in the amount of \$1,143,249.

11. That net operating income of \$1,143,249 for the future test period will result in a return of 4.10% on adjusted gross operating revenues of \$27,872,478 under the fare structure proposed by the staff, and a return of 7.14% on the rate base of \$16,016,810.

#### Conclusions

Upon consideration of the record in this proceeding and the specific Findings hereinabove made, the Commission concludes:

1. That the gross operating revenue method should be utilized to fix rates in this proceeding.

2. That system operating revenues applicable to mass transportation operations for the future test period, in the amount of \$26,708,655, afford a proper basis for measuring the Company's level of earnings at present fares, under the gross operating revenue method for fixing rates.

3. That the "rate base-rate of return" method of fixing rates affords a sound basis for testing the reasonableness of the rate of return computed under the gross operating revenue method of fixing rates.

4. A return of \$660,146 for the future test period at present fares, equivalent to a rate of return of 2.47% on gross operating revenues of \$26,708,655, or 4.12% on a rate base of \$16,016,810, is below the range of what we consider to be a fair and reasonable return and, accordingly, the Company is entitled to some increase in rates.

5. That the fare structure proposed by the Company of a 25 cent cash fare during weekday rush hours, a 20 cent cash fare during all other periods, and a 10 cent school fare would not be in the public interest and should be rejected because it would be discriminatory and the resulting return would be excessive under either the gross operating revenue method or rate base method of fixing rates.

6. That the alternate fare structure proposed by the Company of a 25 cent cash fare, tokens at 5 for \$1.10, and a 10 cent school fare would not be in the public interest and should be rejected because the resulting return would be excessive under either the gross operating revenue or rate base method of fixing rates.

7. That the fare structure proposed by the Company of a 25 cent cash fare, and a 10 cent school fare, to become effective November 1, 1960, should be rejected because estimates of revenues and expenses beyond a future twelve month period are so conjectural as to be unreliable as a basis for fixing rates.

8. That the net operating income of \$1,143,249, for the future test period, resulting from the fare structure proposed by the staff of the Commission of a 25 cent cash fare, tokens at 5 for \$1.00, and a 10 cent school fare, together with a comparable increase in fares from the Company's other mass transportation operations, will provide the Company with a fair rate of return as measured on either the gross operating revenue or the "rate base-rate of return" method of rate-making.

9. That a return of \$1,143,249, equivalent to a rate of return of 4.10% on gross operating revenues or 7.14% on rate base, falls within the range of what we consider to be a fair rate of return and will enable the Company to meet its interest requirements, to pay reasonable dividends, to permit retention of a reasonable proportion of earnings in the business, to provide a margin for unforeseen contingencies, and to attract the necessary capital to meet its future capital requirements.

10. That a District of Columbia fare structure consisting of a 25 cent cash fare, tokens at 5 for \$1.00, and a 10 cent school fare, affords a practical method of fare collection, is just, reasonable, and non-discriminatory and should be approved.



NOW, THEREFORE, IT IS ORDERED:

That effective on and after 4:00 a.m., Sunday, March 6, 1960, the present schedule of fares for D. C. Transit System, Inc., for transportation of passengers within the District of Columbia is hereby cancelled, and that the said Company is hereby authorized and directed to charge the following rates of fare for transportation of passengers within the District of Columbia:

Cash Fare - 25¢

Token Fare - 20¢, to be sold in units of 5 for \$1.00

School Fare - 10¢, with tickets to be sold in units of 10 for \$1.00 or 20 for \$2.00.

By the Commission:

Norman B. Belt  
Executive Secretary

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

March 31, 1960

IN THE MATTER OF

Petition of D. C. TRANSIT SYSTEM, INC.  
For Change in Schedule of Rates.

} P. U. C. No. 3628  
} Formal Case No. 471

OPINION IN SUPPORT OF  
FINDINGS, CONCLUSIONS, AND ORDER  
PROMULGATED MARCH 2, 1960  
(Order No. 4631)

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On March 2, 1960, the Commission promulgated Order No. 4631 wherein it set forth its Findings and Conclusions. On the basis of said findings and conclusions the Commission ordered the Company to cancel the schedule of fares then in effect and to charge on and after 4:00 a.m., Sunday, March 6, 1960, the following rates of fare for transportation of passengers within the District of Columbia:

Cash Fare - 25¢

Token Fare - 20¢, to be sold in units of 5 for \$1.00

School Fare - 10¢, with tickets to be sold in units  
of 10 for \$1.00 or 20 for \$2.00

In said Order No. 4631 the Commission stated that time did not permit the preparation and issuance of an opinion in the detail usually promulgated by the Commission in rate proceedings and that detailed reasons supporting the findings and conclusions therein made would be filed as promptly as possible after March 6, 1960.

Pursuant thereto the Commission sets forth below the detailed reasons upon which its Findings, Conclusions, and Order were predicated.

Utilization of Gross Operating Revenue Method of Rate Making

The Company has contended in this proceeding that its rates should be established under the gross operating

revenue method.<sup>1</sup> In support of its contention the Company cites Section 4 of Public Law 757, 84th Congress, 2d Session (70 Stat. 598), approved July 24, 1956 (hereinafter referred to as the "Franchise Act"). Section 4 provides as follows:

"It is hereby declared as a matter of legislative policy that in order to assure the Washington Metropolitan Area of an adequate transportation system operating as a private enterprise, the Corporation, in accordance with standards and rules prescribed by the Commission, should be afforded the opportunity of earning such return as to make the Corporation an attractive investment to private investors. As an incident thereto the Congress finds that the opportunity to earn a return of at least 6-1/2 per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on either the system rate base or on gross operating revenues would not be unreasonable, and that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible and as conditions warrant; and if conditions warrant not later than August 15, 1958.\*\*\*"  
(Emphasis supplied)

This Commission in the past has employed the rate base method in fixing the rates to be charged by this Company and its predecessor, Capital Transit Company. The use of the gross operating revenue method of rate making in the District of Columbia was proposed for the first time under Public Law 757. Since the enactment of the Franchise Act the Company has repeatedly urged this Commission to adopt the gross operating revenue method. The Commission was requested by the Company to adopt the gross operating revenue method in the Company's first rate proceeding filed on May 2, 1958. In that proceeding (Formal Case No. 460) the Commission in its "Findings of Fact and Conclusions" promulgated August 28, 1958, stated:

"The Company proposed that the determination in this proceeding should be made under the operating ratio method whereby it would be afforded the opportunity of earning 6-1/2 per cent on gross operating revenues, even though rates were not requested in this proceeding to provide such a return. The testimony of both of the staff witnesses was to the effect that the adoption of the

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<sup>1</sup>Although the Franchise Act speaks of a return on gross operating revenues, this is merely another way of referring to operating ratio.

"operating ratio method was directly related to the conversion requirement of Section 7 of the Franchise Act, and the related increase in the investment incident thereto. It was their opinion that the conversion program has not progressed to the point where conditions at this time warrant shifting to the operating ratio method. In this we concur, and accordingly find that present conditions do not warrant shifting to such gross operating base method."

On January 14, 1959, the Company by letter (Exhibit No. 3) requested a decision from the Commission as to when it would approve the adoption of the gross operating revenue method for the determination of the return to be earned by the Company. On January 27, 1959, the Commission replied (Exhibit No. 5) in part as follows:

"\* \* \* It is the considered view of the Commission that the major conditions to be met by the Company before a shifting to gross operating revenue method is warranted, would include compliance with the following:

"(1) A conversion of street railway operations to bus operations measured by abandonment of not less than 55 per cent of street railway track on the basis of mileage; or

"(2) Completion of not less than 51 per cent of the conversion program as measured on the basis of new buses purchased (or committed to be purchased) to replace retired street cars; and

"(3) Adoption of a firm program of gradually replacing existing buses which are more than 16 years of age. \* \* \* "

The Commission has been mindful of the legislative policy as enunciated by Congress in Section 4 of the Franchise Act that we should encourage and facilitate a shifting from the system rate base to the gross operating revenue base "as promptly as possible and as conditions warrant." It is apparent from the very language of the Franchise Act that Congress intended for this Commission to adopt the gross operating revenue method, leaving to us the sole duty of determining the time when such adoption should take place. In other words, Congress has charted a course which this Commission can postpone for cause but cannot change.

In light of the declaration of Congress, we are unable to reconcile the opposition of some of the parties in this proceeding to utilizing the gross operating revenue method of fixing rates. An intervenor's witness (Dr. Ezekiel Limmer) testified that, although he had not read the Franchise Act, he opposed the theory of the gross operating revenue method in rate proceedings, and that such method would not be "proper" or "warranted" at any time under any conditions even though he was aware of the fact that for many years the Interstate Commerce Commission has employed gross operating revenues in fixing motor bus rates. The same witness testified that the gross operating revenue method is nothing more than a cost plus method and therefore undesirable. The validity of this argument is open to question for, in the final analysis, every rate determination is nothing more than the sum of cost plus a reasonable profit.

The Commission does not feel that it is necessary in this proceeding to discuss or to pass upon the merits of the gross operating revenue method of rate fixing.<sup>2</sup> Suffice it to say, it is the opinion of the Commission that the Franchise Act explicitly prescribes the use of the gross operating revenue method as soon as possible and as conditions warrant, and accordingly, this Commission has no recourse but to adopt such method if conditions warrant. The Franchise Act did not enumerate the conditions which would warrant the adoption of the gross operating revenue method. Our problem therefore has been to determine the intent of Congress as to just what conditions would warrant a shifting to the gross operating revenue method and to determine whether the Company has met those conditions.

The Commission in its letter to the Company of January 27, 1959, laid down two conditions that should be met before a shifting to the gross operating revenue method would be warranted, namely: that the Company would have to (1) make substantial progress in converting street railway operations to bus operations, and (2) adopt a firm program of gradually replacing existing buses which are more than 16 years of age.

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<sup>2</sup>We are aware that the gross operating revenue has been used by the Interstate Commerce Commission and by many state regulatory commissions to regulate the motor carrier industry. These state commissions include California, Connecticut, Florida, Hawaii, Illinois, Indiana, Kentucky, Maine, Massachusetts, Michigan, Utah, Washington, and Wisconsin. We are also aware of the fact that the ordinary "rate base-rate of return" approach to allowable earnings is not as reliable a gauge in the case of a transit company as it is in the case of electric, gas, and telephone utilities, for the reason that the revenues and expenses of transit companies are both relatively high as measured against their plant accounts.



With respect to the first condition, the Commission specified that conversion to bus operations would be deemed substantial if (a) not less than 55 per cent of the street railway track was abandoned, or (b) if not less than 51 per cent of the conversion program as measured on the basis of new buses purchased or committed to be purchased to replace retired street cars was completed.

The evidence of record in this proceeding shows that before the close of the hearing the Company had successfully met both of the foregoing considerations relating to conversion. With respect to track abandonment, the record shows that by January 3, 1960, the Company had abandoned 61.1 per cent of street railway track on the basis of mileage (Exhibit No. 6), or 6.1 per cent more than required by the Commission. With respect to new buses purchased to replace retired street cars, the record shows that 100 new buses were delivered in the fall of 1958, that 75 new buses were delivered in the fall of 1959, that 25 new buses were scheduled for delivery before the end of 1959,<sup>3</sup> and that 100 new buses were scheduled for delivery in the spring of 1960.<sup>4</sup> The first two deliveries, aggregating 175 buses, constituted 55.5 per cent of the buses required to replace street cars, or 4.5 per cent more than required by the Commission. With the delivery of the next 25 buses, the aggregate of 200 buses constituted 63.5 per cent, or 12.5 per cent more than required by the Commission. With the delivery of the next 100 buses, the aggregate of 300 buses will constitute 95.2 per cent, or 44.2 per cent more than required by the Commission. On the basis of the foregoing the Commission finds that the Company has complied with the condition relating to the conversion of street railway operations to bus operations.

With respect to the second condition, that the Company adopt a firm program of gradually replacing existing buses which are more than 16 years of age, the record discloses that in addition to the 100 buses presently on order for delivery in the spring of 1960 the Company during the course of the hearings, through its witness Flanagan committed itself to a firm program of purchasing 100 buses in 1961 and 100 buses in 1962. Staff witness Falk questioned the adequacy of the Company's replacement program and pointed out that at the end of 1962 when the conversion program is scheduled for completion there will still be 175 buses more than 20 years of age. He testified that the replacement program to which the Company is now committed was inadequate

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<sup>3</sup>The Commission is advised that this group of 25 buses was placed in service on January 3, 1960.

<sup>4</sup>The Commission is advised that this group of 100 buses will be placed in service during March 1960.



and recommended that the Company be required to commit itself to purchase 125 buses in each of the years 1961, 1962, and 1963.

We agree with the staff that a more extensive replacement program than that proposed by the Company would be desirable, both from the standpoint of benefit to the riding public in comfort and service and to the Company in economy and efficiency of operation, but we believe it would be unwise to require the Company to commit itself at this time to making heavy capital outlays for a period in the future when operating revenues and expenses cannot be forecast with any reasonable accuracy. We believe that the sounder course to follow is to adopt a replacement program which the Company can meet financially and which has a reasonable assurance of being successfully attained. The Commission will adopt a policy of making a continuous study of the need for replacing over-age buses and, as well, of the financial ability of the Company to satisfy such need. If, in the future, the need for new buses becomes more acute than at present the Commission will initiate appropriate action to require the Company to step up its replacement program. Moreover, we cannot foresee the possible effect on the Company of legislation pending in the Congress to create a temporary National Capital Transportation Agency and to authorize creation of a National Capital Transportation Corporation. Until present plans to develop a unified and integrated system of transportation for the National Capital Region progress to the point when the impact of such plans on private transit can be evaluated, we believe it desirable to adopt a moderate policy in the area of bus replacement. On the basis of the foregoing the Commission finds that the Company has substantially complied with the condition that it adopt a firm program of gradually replacing existing buses which are more than 16 years of age.

After giving careful study to the provisions of the Franchise Act, and after careful consideration of the evidence of record bearing on the issue of whether the gross operating revenue method should now be adopted in fixing the rates of the Company, the Commission finds that the Company has complied substantially with the intent of the Franchise Act and with the conditions heretofore indicated by the Commission as warranting the utilization of the gross operating revenue method for rate making purposes in keeping with the legislative policy declared in Section 4 of the Franchise Act, and concludes that the gross operating revenue method should be utilized to fix rates in this proceeding.

The Company has contended that adequacy of earnings should be measured entirely on the basis of gross operating revenues. Although we have concluded that the gross operating revenue method should be utilized to fix rates in

this proceeding, we do not agree with the contention that the gross operating revenue method should be the sole determinant of the reasonableness of rates. The gross operating revenue method and the "rate base-rate of return" method are both valuable indices of the reasonableness of the earnings of a transit company. We have long recognized that the theory employed in determining the amount of revenue required by a transit company is immaterial so long as the end result -- the amount allowed -- is adequate to enable the Company to meet its interest requirements, to pay reasonable dividends, to permit retention of a reasonable proportion of earnings in the business, to provide a margin for unforeseen contingencies, and to attract the necessary capital to meet its future capital requirements. In utilizing the gross operating revenue method we fully recognize the need for checking the reasonableness of the return earned under that method. All of the witnesses on this subject agreed that there is no formula for determining what constitutes a fair return on gross operating revenue, and that such return must, of necessity, be the result of Commission judgment in relationship to the facts surrounding a particular situation. Where judgment must be used, it is desirable to apply checks thereon if proper and related checks are available. The witness Roberts for the staff of the Commission testified that due regard should be given to the rate of return that would be earned on the rate base as a check on the reasonableness of the rate of return computed under the gross operating revenue method. The Commission notes that other jurisdictions have pointed out the desirability of utilizing the rate of return on rate base as a check on the reasonableness of the rate of return computed under the gross operating revenue method. Where a rate base is available, as in the case here, such a check can be readily made, thereby furnishing an appropriate means of measuring the reasonableness of the rate of return computed under the gross operating revenue method. On the basis of the foregoing, the Commission finds that the "rate base-rate of return" method of fixing rates affords a sound basis for testing the reasonableness of the rate of return computed under the gross operating revenue method of fixing rates, and concludes that the "rate base-rate of return" method should be employed in this proceeding to test the reasonableness of the rate of return computed under the gross operating revenue method. Accordingly, we deem it necessary in this proceeding to make a rate base determination.

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(d) Depreciation and Amortization

Depreciation  
Amortization of Acquisition Adjustment  
Provision for Track Removal and Repaving

The three foregoing items are in a number of respects related, particularly in the treatment accorded them by the witness for the intervenors, and neither item can be considered entirely independent of the other two. We will, accordingly, discuss all three items in this section of our opinion. However, since the recommendations of the intervenors' witness differ so materially from those of the Company witness and the staff witness, we will first discuss the differences in the proposals of the latter. The results of their recommendations are summarized as follows:

	Company Witness <u>Exhibit 10-A</u>	Staff Witness <u>Exhibit 39</u>
Depreciation based on Original Cost	\$ 2,987,925	\$ 2,691,015
Amortization of Acquisition Adjustment	-1,033,904	-1,033,904
Provision for Track Removal and Repaving	<u>1,044,196</u>	<u>1,044,196</u>
Total Depreciation and Amortization	\$ <u>2,998,217</u>	\$ <u>2,701,307</u>

From the above summary, it can be seen that the provision for depreciation and amortization proposed by the Company witness exceeds that of the staff witness by \$296,910, and this difference is related wholly to the provision for depreciation. With respect to the other two items, the proposals by both witnesses are in accordance with directives heretofore issued by this Commission and discussed fully in our Findings and Certification issued under date of November 27, 1957, P.U.C. No. 3592-57, in the matter of determining the Company's liability for motor vehicle fuel taxes for the twelve months ended August 31, 1957, under the provisions of Section 9 of the Company's franchise.

Briefly, the credit for amortization of acquisition adjustment in the amount of \$1,033,904 is the annual write-off of the total amount of \$10,339,041, which is the excess of depreciated original cost of road and equipment acquired by D. C. Transit System, Inc. from Capital Transit Company over that portion of the purchase price assignable to road and equipment. The record shows that the amortization of this excess over a ten-year period was adopted in lieu of

distributing the purchase price of the property over all of the items of property acquired. That is to say, the property is recorded on the books of D. C. Transit System, Inc. at original cost to Capital Transit Company, in accordance with the provisions of the Uniform System of Accounts, and depreciation is accrued on the basis of original cost, with an offsetting credit for amortization of the acquisition adjustment to effectively reduce the provision for depreciation to the basis of depreciation on the purchase price of the property. We approved this procedure in the 1958 rate proceeding and in prior motor vehicle fuel tax determinations and find no reason for changing that position for purposes of this proceeding.

Provision for track removal and repaving in the amount of \$1,044,196 represents the annual provision for the cost of track removal and repaving estimated at a total cost of \$10,441,958, said total cost to be provided equally over a ten-year period from August 15, 1956. The estimated total cost of track removal and repaving is based on the average of a Company estimate of \$11,883,916 and an estimate by the staff of the Commission of \$9,000,000, in both instances contemplating complete removal of the entire track structure.

A question has been raised by intervenors in this proceeding as to why funds provided for track removal and repaving are not segregated in a separate fund and invested in such a way as to earn interest which might be applied to reducing track removal and repaving costs to be charged to the customers. The Commission has given full consideration to the matter of segregating these funds in the past, and in recognition of the Company's cash needs in connection with acquisition of new buses, it was concluded that the public interest would be served by not requiring segregation of cash funds in a separate cash account. We find nothing in this record to justify a different conclusion at this time.

A question has also been raised with respect to the adequacy or inadequacy of the provision that is presently being made for track removal and repaving. Up to the present time, there has been only a limited amount of track removal and repaving work undertaken, so that sufficient data are not now available for testing the adequacy or inadequacy of the provision. The Commission recognizes that the provision now being made is based on engineering estimates which may prove to be either excessive or deficient by actual experience. We have indicated our intention of keeping this matter under study with a view to making such adjustments as might be found appropriate in the future. Pending further experience, we find for purposes of this proceeding that the annual provision of \$1,044,196 for track removal and repaving is reasonable.



Reference is now made to the item for depreciation based on original cost of the property, wherein the estimate of the Company witness exceeds that of the staff witness by \$296,910. The estimates of both witnesses are based primarily on depreciation rates prescribed by this Commission, which became effective as of July 1, 1953, by Order No. 4001. While there are minor differences in the estimates by the two witnesses with respect to depreciation to be allowed on new buses to be acquired, and with respect to old buses scheduled for retirement during the year 1960, the major difference in the two estimates is related to the provision for extraordinary retirement losses incident to conversion from rail operations to bus operations that have already been and will be undertaken prior to August 15, 1963, under the provisions of the franchise.

As shown by the Company Exhibit No. 10-A, the estimated net undepreciated cost of rail facilities as of December 31, 1959, amounts to \$5,121,644, and it was proposed by the Company witness that this amount be fully recovered over the remaining 43.5 months of the conversion period from January 1, 1960 through August 15, 1963. This would require a monthly provision of \$117,738.94 instead of the present provision of \$67,891.25 under rates prescribed by this Commission, an increase of \$49,847.69 per month or \$598,172 on an annual basis.

The staff witness agreed with the Company estimate of net undepreciated cost as of December 31, 1959, in the amount of \$5,121,644, and that the Company is entitled to recover this amount over some future period. It was his position, however, that to make provision for recovery of the entire amount over the remaining 43.5 months of the conversion period would place too heavy a burden on the customers during this period. It was his proposal that we now make provision only for that portion of the undepreciated cost that is associated with the track facilities that were abandoned on January 3, 1960. Using a factor of 49.40% based on the relation of the single track footage of rail facilities abandoned on January 3, 1960, to total track footage prior to that date, the undepreciated cost on these facilities would amount to \$2,530,092. On this basis, additional provision of \$295,500 per annum would be required over and above the provision presently being made on total rail facilities as of December 31, 1959. His estimate of depreciation for the future annual period in the amount of \$2,691,015 reflects this additional provision of \$295,500, instead of the Company proposal of \$598,172.

With respect to the undepreciated cost related to the remaining track facilities, it was the recommendation of the staff witness that provision should be made for recovering these costs in the light of conditions existing at the

time these facilities are actually abandoned. He directed attention to the fact that the depreciation study used as a basis for determining the estimated undepriciated cost of rail facilities as of December 31, 1959, was completed in the early part of 1953, and that it is quite possible that a current study might result in a somewhat different determination of the amount of unrecovered depreciation assignable to these track facilities. The record also shows that under the group method of depreciation provided for in our Order No. 4001, approximately \$1,200,000 of depreciation over and above original cost has been accrued on buses that have exceeded their estimated normal service life of 14 years. The staff witness proposed that any excess accruals applicable to over-age buses might well be applied as a partial offset to any unrecovered depreciation related to rail facilities that might be disclosed by a depreciation study.

It is the opinion of the Commission that until such time as a new depreciation study is made, and until we have had sufficient experience with the actual cost of track removal and repaving work to test the adequacy or inadequacy of the present provision for track removal, the additional provision of \$295,500 recommended by the staff witness is as far as the Commission should go at this time in making separate provision for extraordinary retirement loss related to track facilities. Numerous precedents can be found where commissions have provided for recovering extraordinary retirement losses resulting from obsolescence over a reasonable period in the future.

The proposals by witness Harris for the intervenors with respect to depreciation and amortization are reflected by his Exhibits Nos. 51-A and 54-A. As shown by Exhibit No. 54-A, the witness has adopted, as a starting base for his determination, the revenues and expenses taken from staff Exhibit No. 39 which shows net operating income of \$660,146. It should be pointed out in passing that the figures taken from Exhibit No. 39 are after allocation to limousine operations and charter and sightseeing operations, whereas the adjustment proposed by witness Harris for bus depreciation, as well as his adjustment for F.I.C.A. taxes heretofore discussed, gives no consideration to the related effect of these allocations.

The witness states that his adjustments are based on a consideration of the adequacy of reserve provisions shown by the books as of September 30, 1959, as a basis for disposing of any remaining value in rail facilities and providing for the cost of track removal and repaving. For purposes of his study, he treats the unamortized balance in the acquisition adjustment account in the amount of \$7,108,091 as a reserve, which together with the actual



balance in the Reserve for Track Removal and Repaving of \$3,216,286 results in a total alleged reserve provision of \$10,324,377. Originally he stated this amount was available for writing off the net undepreciated cost of rail facilities as of September 30, 1959, in the amount of \$5,121,644, with the remainder being available to provide for the total estimated cost of track removal and repaving on a net of taxes basis, as shown by his Exhibit No. 51. Subsequently he submitted a revised Exhibit, No. 51-A, showing that his alleged reserve provision was insufficient to meet the total cost of track removal and repaving to the extent of \$1,264,515.

The witness further states that his proposals were not related to any consideration of the conditions of the agreement dated July 7, 1956, whereby D. C. Transit acquired all of the assets of Capital Transit Company. Based on our reading of the record, however, we can reach no other conclusion but that his proposals are based in large measure on his speculation of what considerations entered the minds of the contracting parties as of July 7, 1956. The record shows that as of the time of testifying, he had not read the agreement and was not familiar with the terms thereof.

The record contains evidence to the effect that the purchase price paid by D. C. Transit of \$13,540,000 was based on a market price of \$14.00 per share for the 960,000 shares of Capital Transit Company common stock outstanding as of the date of the agreement, plus an additional amount of \$100,000 to meet an offer of another prospective purchaser. What other considerations may have entered the minds of the contracting parties is not a matter of record. Mr. Harris has concluded, however, that the purchase price paid by Mr. Chalk as a prudent investor was based on writing off all rail facilities as being of no value and that the purchase price also reflected the liability of the Capital Transit Company for track removal and repaving, which he states was assumed by D. C. Transit.

We fail to see how rail facilities could be considered as valueless when they had a remaining useful life of seven years and were at the time producing annual revenues of approximately \$12,000,000. Furthermore, while recognizing that the obligation for track removal and repaving may have had some bearing on the fact that the property was acquired at substantially less than the net depreciated original cost, we have been unable to find any evidence as to the extent of its effect in dollars on the purchase price.

The witness relies in large measure for his conclusions with respect to the considerations that entered the minds of the contracting parties on the testimony of the

Company's Vice President and Comptroller in the 1958 rate proceeding, an excerpt from which is attached to his Exhibit No. 51-A. He fails to recognize that this testimony by Mr. Flanagan was in support of a proposal by the Company in that proceeding that the Company's rate base should be based upon the net depreciated original cost of the property in the amount of approximately \$18,000,000, instead of the purchase price rate base proposed by the staff of the Commission in the approximate amount of \$8,000,000. The fact is that the Company proposal in the 1958 rate proceeding was rejected by the Commission which adhered to the accounting for both acquisition adjustment and track removal and repaving it had previously prescribed. This accounting was adopted by the other two witnesses for purposes of this proceeding.

The record does not disclose, under the Harris proposal, the source of the cash funds that will initially be required for track removal and repaving in the estimated total amount of \$10,441,958. An amount of \$3,524,161 has been provided during the period from August 15, 1956 through December 31, 1959, under accounting prescribed by the Commission. Since his proposed allowance of \$1,264,515 on a net of taxes basis would provide cash funds prior to income taxes of only \$2,767,888, it is not clear where the remaining cash funds of \$4,149,909 will come from.

One other area in which the witness has proposed adjustments based upon accounting treatment contrary to that prescribed by outstanding orders of this Commission is in the matter of depreciation for buses. He has proposed that the unit method of depreciation be applied with respect to buses that are more than 14 years of age, in lieu of the group method of depreciation presently in effect. Under the group method of depreciation, which method is used extensively in utility regulation, rates are based upon average service lives for the various classes of property. These rates are applied to the original cost of depreciable property so long as the property remains in service, the assumption being that accruals on property lasting beyond the estimated service life will offset deficiencies in accruals on property retired prior to reaching the average service life.

The witness Harris also proposed a curious modification of the group method of depreciation which he claimed would accomplish the same results as the unit method, but under questioning he admitted that so far as he is aware no regulatory agency has adopted his proposed method. The method which he proposed would be applied to bus property alone and would give no consideration to the effect of premature retirements in other classes of property, particularly rail property. Under his proposal depreciation on

buses would be reduced under the allowance proposed by the staff by \$246,253. The Commission has been fully advised in this matter and is of the opinion that no change should be made in the prescribed group method of depreciating property, including buses, pending a complete study of the status of the existing depreciation reserve with respect to all depreciable property.

After full consideration of the proposals by the various witnesses with respect to depreciation, amortization of acquisition adjustment, and provision for track removal and repaving, we adhere to our previously prescribed accounting treatment of these items, modified only with respect to the provision for extraordinary retirement loss on abandoned rail facilities as of January 3, 1960. Accordingly, we find that the proposed allowance for depreciation and amortization in the amount of \$2,701,307, heretofore summarized, is just and proper. We reserve for future decision a determination as to what provision should be made with respect to any additional extraordinary property loss until such time as a depreciation study has been completed and the remaining rail facilities have been abandoned.

\* \* \*

(f) Allocation to Limousine and to Charter and Sightseeing Operations

Exhibit No. 39 shows the allocation of revenues and expenses to limousine operations and to charter and sightseeing operations proposed by the staff witness, which are summarized as follows:

	<u>Limousine Operations</u>	<u>Charter and Sightseeing Operations</u>
Operating Revenues	\$ 88,592	\$ 864,277
Operating Revenue Deductions:		
Operating Expenses	\$102,428	\$ 874,851
Taxes, other than income taxes	3,449	41,023
Income taxes	- 19,984	- 50,592
Depreciation and amortization	34,911	40,737
Total	120,804	906,019
Net Operating Income (Deficit)	\$- 32,212	\$- 41,742

Operating revenues from these operations are accounted for directly on the books of the Company and require no allocation. The schedules supporting Exhibit No. 39 show the basis for the allocations of adjusted operating revenue deductions to these operations. The allocation of expenses was based on a "full cost" allocation method, and while the Company witness contended that this method results in overstating expenses chargeable to these operations, he accepted the method for purposes of this proceeding. The negative amounts shown for income taxes are intended to give these operations the benefit of the reduction in income taxes resulting from the estimated loss prior to income tax accruals.

No party to the proceeding questioned the results of the allocations made to limousine operations and to charter and sightseeing operations, and we find the operating results for these operations as shown by Exhibit No. 39 to be proper for purposes of this proceeding.

(g) Results of Mass Transportation Operations

Based on all of the foregoing and a full consideration of the record, we find that system operating revenues applicable to mass transportation operations for the twelve months ending December 31, 1960 at present fares are properly estimated to be \$26,708,655, and that net operating income applicable to mass transportation operations for the same period at present fares, is properly estimated to be \$660,146.

RATE BASE DETERMINATION

Testimony was offered by staff witness Falk on the net investment rate base to be used as a basis for testing the reasonableness of the Company's projected earnings for the twelve months ending December 31, 1960, under the traditional "rate base-rate of return" method of rate making. His testimony was supported in detail by Schedule 4 of Exhibit No. 39, wherein he proposed a rate base of \$16,016,810 based upon giving equal weight to the net investment in rate base property based on original cost and based on purchase price. The development of this rate base is summarized as follows:

Based on Original Cost:

Investment in Road and Equipment at Original Cost	\$ 49,818,778
Plus Construction Work in Progress	467,752
	<u>50,286,530</u>

Less the Reserve for Depreciation	-31,476,647
	<u>18,809,883</u>
Plus the Investment in Materials and Supplies	774,508

Net Investment in Property applicable to Total Operations	19,584,391
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Less the Investment in Property devoted to Other than Mass Transportation Operations:	
Limousine Operations	- 87,806
Charter and Sightseeing Operations	- <u>355,078</u>

Net Investment in Rate Base Property based on Original Cost	\$ <u>19,141,507</u>
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Based on Purchase Price:

Investment based on Original Cost	\$ 19,141,507
Less the balance in Account 401.3 - Acquisition Adjustment (Credit):	
Applicable to Total Operations	\$ 6,332,663
Less Allocation to Charter Operations	- <u>83,268</u> - <u>6,249,395</u>
Net Investment in Rate Base Property based on Purchase Price	\$ <u>12,892,112</u>

Average of Original Cost and Purchase Price	\$ <u><u>16,016,810</u></u>
---	-----------------------------

The Company witness presented no evidence to develop a net investment rate base for purposes of this proceeding, it being his position that rates should be established solely on the basis of gross operating revenues. He did state that if an investment rate base is adopted, it should be based on the depreciated original cost of property to comply with promises made to the Company by Congress and the D. C. Commissioners at the time of granting D. C. Transit its franchise. In our Order No. 4480 in the 1958 rate proceeding, we fully discussed this matter and stated that we found no evidence of record to support the Company contention. No evidence has been presented in this proceeding to change our views on this matter.

Intervenors' witness Harris recommended a rate base of \$12,041,217 as of September 30, 1959, as shown by his Exhibit No. 52, based on the net investment in road and



equipment as of that date, adjusted to exclude the undepreciated cost of rail facilities as of December 30, 1959, in the amount of \$5,121,644 as shown by Company Exhibit No. 10-A. The witness subsequently modified his recommended rate base figure to \$12,643,000 to give effect to projected changes in net investment during the fifteen-month period from September 30, 1959 to December 31, 1960. In making this adjustment, he used figures taken from staff Exhibit No. 39, which figures already had been weighted for the estimated period in service, and, in effect, duplicated such weighting by averaging the resulting balance as of December 31, 1960 and that of September 30, 1959. He then related this rate base, without any allocation of investment to limousine or to charter and sightseeing operations, to his net operating income for the twelve-month period ending December 31, 1960, after allocation to limousine and to charter and sightseeing operations. In view of these inconsistencies, and further in view of our reasons heretofore set forth for rejecting his contention that the rail facilities were valueless as of August 15, 1956, we cannot accept the rate base recommendations of this witness.

The basis for the various elements of cost entering into the staff's rate base was fully covered in the testimony of the witness Falk. The original cost shown for road and equipment represents actual costs recorded on the books of D. C. Transit and its predecessor Capital Transit Company in accordance with the Uniform System of Accounts prescribed by this Commission. Construction Work in Progress was included in the rate base in lieu of accruing interest during construction which would have been capitalized along with other costs, and thus would have been subject to depreciation and return over the life of the property. This practice has been consistently followed in prior transit rate proceedings, and for a number of years in our electric company rate proceedings. We believe it is proper here. The amount deducted as the balance in the depreciation reserve reflects accruals recorded on the books at depreciation rates prescribed by this Commission. The inclusion of the recorded investment in materials and supplies, with no allowance for cash working capital, is consistent with accepted practices of this Commission and many other regulatory agencies. It is a proper element of value to be included in the rate base.

In arriving at the purchase price rate base, the amount deducted as the unamortized balance of the acquisition adjustment (credit) also reflects an amount recorded on the books of the Company, adjusted for estimated changes during 1960, in accordance with prior directives of this Commission.



It can thus be seen that all of the elements of value considered by the staff witness were based on actual amounts recorded on the books of the Company, with appropriate adjustments for estimated changes during the twelve months ending December 31, 1960.

The witness Falk also made allocations to exclude the estimated portions of the various elements of value that were devoted to limousine operations and to charger and sightseeing operations. There was no dispute as to the method used or the result of these allocations as a basis for arriving at the net investment in rate base property applicable to mass transportation operations, on either the original cost or the purchase price method. We find that the allocation is proper.

We find that the net investment of \$19,141,507 based on original cost and the net investment of \$12,892,112 based on purchase price, as shown by Schedule 4 of Exhibit No. 39, are proper elements of value, and that they should be considered in determining a system rate base for purposes of this proceeding.

This Commission has for many years considered the net original cost rate base as a proper method of fixing rates, provided a rate of return is applied to such rate base that will result in a return sufficient to meet the requirements of a fair return to the utility. Such a method has been sustained by the courts. Prior to the acquisition of the assets of Capital Transit Company by D. C. Transit in August of 1956, original cost had been synonymous with purchase price in regulating the utilities under our jurisdiction. However, in view of the purchase of the road and equipment in 1956 at a price substantially below the original cost to the predecessor company, consideration of purchase price is required for a proper balancing of customer and investor interests.

In support of his recommended rate base of \$16,016,810, the staff witness testified that he has proposed averaging the investment based on original cost and the investment based on purchase price to conform with procedure adopted by this Commission in the 1958 transit rate proceeding, as well as in three determinations of the Company's liability for motor vehicle fuel taxes under the requirements of Section 9(c) of the franchise. On Page 5 of our findings and conclusions accompanying Order No. 4480, dated August 28, 1958, we set forth our reasons for adopting such a rate base.

Stated briefly, we there concluded that neither the net original cost nor the purchase price should be considered as the dominant factor nor the exclusive measure of

the Company's property for rate-making purposes. We recognized that the purchase price rate base gives no consideration to the effect, if any, on the purchase price of the assumed liability for track removal and repaving, nor to the fact that the sale was made by Capital Transit Company at a time when the loss of its franchise was imminent with the possibility of being required to dispose of its property in liquidation. On the other hand, a rate base giving consideration only to original cost of the property would ignore the fact that the property was acquired by the present owners at substantially less than the amount at which it was carried on the books of Capital Transit Company, irrespective of the considerations that may have entered the minds of the contracting parties in arriving at the agreed purchase price.

We accordingly concluded that a proper balancing of the interests of both the customers and the investors required us to exercise the latitude which the law allows us in the determination of fair value, and that a rate base giving equal weight to original cost and to purchase price would be fair and reasonable. We find nothing in our consideration of the record in this proceeding to justify a different conclusion at this time.

We have heretofore found that conditions presently warrant changing over to the gross operating revenue base for purposes of this proceeding, and that the "rate base-rate of return" method should be employed to test the reasonableness of the return computed under the gross operating revenue method. Accordingly, we find that a rate base in the amount of \$16,016,810 is a proper rate base applicable to mass transportation operations for the twelve months ending December 30, 1960, and we conclude that it affords a sound basis for testing the reasonableness of a return computed under the gross operating revenue method.

\* \* \*

#### Determination of Fair Return

For the first time the Commission is confronted with the problem of determining a fair return under the gross operating revenue method, commonly referred to as the operating ratio method. A measure of what constitutes such a fair return was expressed by staff witness Edward A. Roberts in the following language "--- out of every dollar taken in by a bus company there should be a few pennies left over, after paying operating expenses and taxes, with which the Company can pay the interest on its indebtedness, dividends to its stockholders and add something to its surplus

account". The record shows that many regulatory commissions have utilized the operating ratio method with varying results. For example, a study by the American Transit Association of 80 decisions shows a wide range of operating ratios from a maximum of 99.8% to a minimum of 87.4%, after taxes. On this point Roberts testified that "--- there is no formula or method of computing how many pennies out of each dollar of revenue should be left over after paying expenses. It seems to be a matter of the exercise of the rate-making authority's best judgment in the light of the facts in the particular case being considered."

In support of his testimony he referred to a 1952 report by a special committee of the National Association of Railroad and Utilities Commissioners which stated, in part, that "--- the level of the operating ratio should be determined with due regard to the conditions prevailing in each case."

Witness Falk testified that a fair return should provide sufficient income, over and above all expenses, to meet interest requirements on debt capital, allow the payment of reasonable dividends, and, in addition, permit the retention of some portion of earnings in surplus. It is our opinion that a return which meets these standards is the fair return which we are required to provide.

As shown by Exhibit No. 39, the net operating income from all operations for the twelve months ending December 31, 1960, at present fares, would amount to \$586,192, and after excluding the loss on limousine operations and on charter and sightseeing operations, the earnings from mass transportation operations would be \$660,146. We find that net operating income of this amount will provide the Company with a return of 2.47% on gross operating revenues of \$26,708,665, and a return of 4.12% on the rate base of \$16,016,810.

Witness Falk testified that interest charges during 1960 would be approximately \$317,000 and if dividends are maintained at the current level another \$500,000 will be required. It was Falk's opinion that without some increase in rates the requirements of a fair return will not be met. In our opinion a return equivalent to 2.47% on gross operating revenues or 4.12% on rate base is below the range of a fair and reasonable return. Accordingly, we conclude that the Company is entitled to some increase in rates.

The District of Columbia fare structure proposed by the staff, together with a comparable increase in fares for the Company's other classes of service, would produce additional net earnings estimated at \$483,103 during the twelve months ending December 31, 1960, as shown on

Exhibit No. 40. These additional earnings, when added to the earnings from mass transportation operations at present fares of \$660,146, result in net operating income under the proposed fare structure of \$1,143,249; equivalent to a return of 4.10% on adjusted gross operating revenue of \$27,872,478 and a return of 7.14% on the rate base of \$16,016,810. In the opinion of the staff witness, net operating income at this level would constitute a fair return. Under the standards which we have heretofore adopted we conclude that a return of \$1,143,249 falls within the range of what we consider to be a fair return.

With earnings at this level, after payment of interest on debt in the estimated amount of \$317,000, approximately \$800,000 would remain available for return on equity capital. This would be a return of approximately 25% on the equity capital recorded on the books as of September 30, 1959, and 30% on equity capital if adjustment, as directed by the Commission, is made to reduce surplus by \$481,212 in connection with the sale of the Company's southwest shop and carhouse property. This adjustment is presently subject to litigation in the courts. Witness Falk testified that such a return on equity capital would fall within the range of a reasonable return when consideration is given to the relatively low percentage of equity capital invested in the business and to the element of risk inherent in any investment in the transit industry. With this the Commission agrees.

A witness for the intervenors, Dr. Ezekiel Limmer, presented a study of the cost of capital to D. C. Transit based primarily on an examination of earnings-price ratios of a number of other transit companies. The only apparent common basis for comparison between his selected group of companies and D. C. Transit is that they all have operating revenues in excess of \$10,000,000 per annum. The wide range of earnings-price ratios for the different companies, as well as from year to year for the same company, is clearly apparent from an examination of his Exhibit No. 43. Based on his study, Dr. Limmer computes the fair return on equity capital for D. C. Transit to be 12.55% after making allowance for financing costs.

This Commission and many other regulatory bodies rely to a large extent upon earnings-price ratios and dividend-price ratios as a guide to the reasonable allowance to be made for return on equity capital in arriving at a fair rate of return for gas and electric companies. Such procedure is appropriate for those types of utilities by reason of their general stability of earnings and dividends, their relative uniformity in capitalization ratios and their large investments in plant per dollar of revenue. This is not the case, however, with respect to transit companies in



general. The Commission, in its Order No. 4052 in the 1953 rate proceeding involving Capital Transit Company, found that the cost of capital method was inappropriate in determining a proper rate of return for a transit company. We find nothing in this record to support a different conclusion.

It is apparent from the record that Dr. Limmer would make no allowance over and above bare cost of capital, a requirement which this Commission and other regulatory bodies have consistently held is necessary in any determination of fair rate of return. Based on his study, he testified that a return of \$652,781 would be sufficient to meet the Company's needs for cost of debt capital and provide a fair return on equity capital. From what we have heretofore stated, it can readily be seen that a return at this level would not cover interest on debt and dividends at their present level. We find that such a return is less than reasonable.

In view of the foregoing, we give little weight to the testimony of Dr. Limmer on the fair return to which the Company is entitled.

The initial fare structure proposed by the Company was estimated by the staff witness to produce net earnings of \$1,617,679, which equates to a return of 5.58% on gross operating revenues of \$29,015,408 and a return of 10.10% on rate base of \$16,016,810. With this amount of earnings, after interest requirements of approximately \$317,000, there would be available for return on equity capital approximately \$1,300,000, or a return on equity of from 41% to 49%, which in the opinion of staff witness Falk would be unreasonably high. With this the Commission agrees.

For the Company, witness Curtin testified that, in his opinion, an operating ratio of 93.5% after taxes was necessary to produce a reasonable return. He based his opinion largely upon a selected list of decisions which were found to be from seven to ten years old. We note that Curtin cited in his list a 1949 finding of the Utah Commission that an operating ratio of 93.3%, after taxes, was reasonable, but he did not list a 1959 finding by that same Commission where a ratio of 95.8% for the same company was found to be reasonable.

Witness Curtin made certain comparisons of the operating ratio of D. C. Transit with those of other major utilities operating in the District of Columbia. Such comparisons may be interesting, but it is our opinion that they fail to shed any light on what constitutes a fair return for D. C. Transit under the operating ratio theory.

It appears that Curtin made no specific study as to the requirements of a fair return for D. C. Transit, separate and apart from the general approach he uses for the transit industry as a whole. From his testimony it is clear that he feels any transit company is entitled to an operating ratio of at least 93.5%, after taxes. With this we cannot agree.

No single rate of return is universally applicable to, or appropriate for, all transit companies. A fair rate of return varies with the conditions and opportunities of a particular company as they exist at the time of a determination. There is no established legal precedent nor any economic formula sufficiently authoritative to be universally applied in a determination of a proper rate of return. What constitutes a reasonable return is a question of fact, the solution of which calls for the exercise of sound judgment and common sense. Our problem here is the specific task of determining a fair return for D. C. Transit, and while the average of ratios allowed in other jurisdictions may give some clue as to the relative position of this Company, it does not, in our opinion, necessarily constitute a fair measure of the needs of this Company.

The fairness of a return is to be tested not alone with reference to the investors, but also to the consumers who are entitled to good service at reasonable rates. We fully recognize that a return too low to provide adequate and efficient transportation service can be as detrimental to the public interests as one that places an excessive burden on the public.

Based on all of the foregoing, the Commission concludes that net operating income of \$1,143,249 for the twelve months ending December 31, 1960, resulting from a District of Columbia fare structure consisting of a 25 cent cash fare, tokens at 5 for \$1.00, and a 10 cent school fare, together with a comparable increase in fares from the Company's other mass transportation operations will provide the Company with a fair rate of return as measured on either the gross operating revenue method or the "rate base-rate of return" method of rate making. Such a return will enable the Company to meet its interest requirements, to pay reasonable dividends, to permit retention of a reasonable proportion of earnings in the business, to provide a margin for unforeseen contingencies, and should enable the Company to attract the necessary capital to meet its future capital requirements.



## Adequacy of Service

In making the findings and conclusions herein set forth we do not disregard our continuing responsibility to see to it that an "adequate transportation system" is maintained. We conceive the definition of adequacy as having to do, among other things, with service. Service has many facets, and a broad comprehensive look must be taken of the picture, not only as it is related to the fare structures, but also as to the quality of service being afforded the community, now and in the foreseeable future. The entire matter must be approached with a realization that the Company has been called upon to convert from streetcars to buses with a seven year period. Section 7 of the Franchise Act reads in part as follows:

Sec. 7. The Corporation shall be obligated to initiate and carry out a plan of gradual conversion of its street railway operations to bus operations within seven years from the date of the enactment of this Act upon terms and conditions prescribed by the Commission, with such regard as is reasonably possible when appropriate to the highway development plans of the District of Columbia and the economies implicit in coordinating the Corporation's track removal program with such plans; except that upon good and sufficient cause shown the Commission may in its discretion extend beyond seven years, the period for carrying out such conversion. \*\*\*

Discounting what we believe to be the improper interpretations that have been placed upon this language to the effect that this Commission can presently postpone or halt the requirement for conversion, we face the issue that adequate service must be maintained while meeting the requirement of conversion. With this in mind, we feel called upon to see that an orderly conversion is effected, and that the substituted bus operation is adequate both as to service and equipment, to meet the public demand. This is our continuing obligation and we shall investigate and act promptly upon any failure of the Company in any of these areas. We shall keep ourselves constantly informed of the quantity and quality of the service which the Company is affording to the public.

In this connection, we feel it is appropriate to comment upon the proposal of the Company to convert its remaining rail operations on January 2, 1962. In our opinion the proposal as submitted is too general and unsupported in detail to warrant any commitment from us as to its desirability or feasibility. We shall require of the Company a

detailed outline of its plans, and if the facts demonstrate a necessity therefor we shall set the matter down for hearing in order that we may have before us as complete a picture as possible to enable us to carry out our function, not only of supervising the conversion from rail to bus as required by Congress, but of performing our duty, of seeing that the Company gives adequate service to the public.

#### CONCLUSION

Having heretofore found that the proposed fare structure consisting of a 25 cent cash fare, a 20 cent token fare, with tokens to be sold in units of 5 for \$1.00, and a 10 cent school fare, applicable to mass transportation operations in the District of Columbia, together with a comparable increase in fares for the Company's other mass transportation operations, will provide the Company with a fair return, and that such fare structure is just, reasonable, and nondiscriminatory, we issued our Order No. 4631 under date of March 2, 1960, prescribing the said fare structure to become effective on March 6, 1960. This opinion is issued in support of Order No. 4631 and the findings and conclusions therein set forth.

A TRUE COPY:     :

By the Commission:

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Norman B. Belt  
Executive Secretary

RELEVANT DOCKET ENTRIES - C.A. 1529-60

1960

- May 20 - Complaint  
\* \* \*
- June 8 - Answer of defendant # 1 (Public Utilities  
Commission)
- June 9 - Answer of defendant # 2 (D.C. Transit)  
to Complaint; Counterclaim vs. plaintiffs
- June 23 - Answer of plaintiffs to counterclaim of  
defendant # 2  
\* \* \*
- July 25 - Motion of plaintiffs for summary judgment  
\* \* \*
- August 22 - Motion of defendant # 2 for summary judg-  
ment on counterclaim
- August 25 - Motion of defendant # 1 to dismiss complaint  
\* \* \*
- September 15 - Order granting motion of defendant # 1 to  
dismiss complaint
- September 17 - Notice of Appeal of plaintiffs  
\* \* \*

1961

- January 31 - Certified copy of judgment of USCA reversing  
and remanding for further proceedings  
\* \* \*

- February 17 - Order vacating dismissal of September 15, 1961; cause to be set for hearing pursuant to provisions of Title 43, Section 705 of D. C. Code
- March 29 - Order denying plaintiffs' motion for summary judgment and denying defendant # 1 motion to dismiss and denying defendant # 2 cross motion for summary judgment
- April 6 - Motion of defendant # 1 to vacate order entered March 29, 1961 and to reconsider and grant motion of defendant # 1 to dismiss
- April 12 - Motion of plaintiffs to reconsider and modify order denying plaintiffs' motion for summary judgment
- \* \* \*
- April 18 - Stipulation dismissing counterclaim of defendant # 2; defendant # 2 may file amended answer
- April 18 - Amended answer of defendant # 2
- April 19 - Amendment of plaintiffs' motion to reconsider and modify order of March 29, 1961
- June 5 - Order vacating order of Court entered March 29, 1961, and denying motion of plaintiffs for summary judgment and granting motion of defendant # 1 to dismiss and affirming Order No. 4631 of Public Utilities Commission dated March 2, 1960
- \* \* \*
- June 26 - Notice of Appeal by plaintiffs
- \* \* \*

[Filed 20 May 1960].

COMPLAINT

I

This is a petition of appeal from Order No. 4631 of the defendant Public Utilities Commission of the District of Columbia (hereinafter the "Commission"), dated March 2, 1960, pursuant to Section 43-705, D. C. Code (1951) which Section confers jurisdiction on this Court. Order No. 4631 authorized an increase in rates of fare charged within the District of Columbia by defendant D. C. Transit System, Inc. (hereinafter "Transit").

II

Each of the plaintiffs are individuals who ride the regularly scheduled vehicles of Transit from place to place in the District of Columbia and are affected by Order 4631 and by the schedule of rates authorized therein since such rates are charged as a condition of riding said vehicles.

III

Defendant Commission is a statutory agency with power and authority to determine the schedule of rates of defendant Transit under Titles 43 and 44 of the D. C. Code (1951), Public Law 757 - 84th Congress (70 Stat. 598) (Hereinafter the "Franchise"), and other laws of the District of Columbia and of the United States.

#### IV

The defendant Transit is a corporation organized under the laws of the District of Columbia. It owns and operates street railway and motor carrier transit properties within the District of Columbia. It is a "public utility" under Title 43 and 44 of the D. C. Code (1951).

#### V

Upon petition of Transit, and after hearings, the Commission issued its Order 4631, dated March 2, 1960, authorizing Transit to charge the following schedule of rates for transportation of passengers within the District of Columbia, effective March 6, 1960:

Cash	-	25 cents
Token fare	-	20 cents, to be sold in units of 5 for \$1.00
School fare	-	10 cents, with tickets to be sold in units of 10 for \$1.00 or 20 for \$2.00.

This schedule of rates is the same as that in effect prior to March 6, 1960, except that the cash fare had been 20 cents.

The Commission on March 31, 1960, issued its "Opinion in Support of Findings, Conclusions, and Order promulgated March 2, 1960 (Order No. 4631)".

#### VI

The plaintiffs on April 1, 1960, duly filed their Petition for Reconsideration of the Commission's Order 4631. On



April 27, 1960, the Commission issued its Order 4645 denying plaintiffs' Petition for Reconsideration.

#### VII

The Commission erred as a matter of law in Order 4631 and its Opinion in Support, and acted arbitrarily, capriciously, unreasonably, without and contrary to the substantial evidence of record, in finding that a return of \$660,146 would be earned during the test period without a fare increase.

#### VIII

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in allowing as revenue deductions excessive accruals for depreciation and any or excessive accruals for track removal and repaving.

#### IX

The Commission erred as a matter of law in Order 4631, and its Opinion in Support, and acted arbitrarily, capriciously, unreasonably, without and contrary to the substantial evidence of record in concluding that the gross operating revenue method should be utilized to fix Transit's rates and in failing to find or conclude that conditions do not warrant the use of such rate-making method.

#### X

The Commission erred as a matter of law in said Order and Opinion and acted arbitrarily, capriciously, unreasonably and

without and contrary to the substantial evidence of record, in failing to conclude that it did not utilize the gross operating revenue method of rate-making within the meaning of Sections 4 and 9 of the Franchise.

#### XI

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in using a rate base giving equal weight to the price by the Transit in 1956 for the properties and to the original cost of the properties to the person first devoting the properties to the public service; and in failing to use as the basis for the rate base the said 1956 purchase price (adjusted to date for additions and retirements of property).

#### XII

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in failing to deduct, in computing rate base, the amounts accrued in the reserves for Track Removal and Repaving, for Injuries and Damages, and for payment of income taxes.

#### XIII

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in

including in rate base property no longer used and useful in the public service.

XIV

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in concluding that a return of 4.10% on gross operating revenues or 7.14% of the system rate base falls within the range of a fair rate of return.

XV

The Commission erred as a matter of law in Order 4631 and its Opinion in Support, and acted arbitrarily, capriciously, unreasonably, without and contrary to the substantial evidence of record, in finding that a return of \$660,146 during the test period was below the range of a fair and reasonable return and that Transit was entitled to an increase in fares.

XVI

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in failing to give effect to the fact that all of Transit earnings are paid out in dividends to its parent company (D.C. Transit System, Inc., a Delaware Corporation) and that its grandparent company (Transportation Corporation of America) is engaged in selling the Delaware company stock, based upon Transit's earn-

ings, at 40 to 50 times its cost, to obtain windfall capital gains which inhibits Transit from raising capital for its public utility needs within the District of Columbia.

#### XVII

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record in failing to give effect to the fact that Transit keeps large deposits in banks without drawing interest and in excluding evidence as to whether officials and stockholders of Transit and its parent and grandparent companies are borrowing money from such banks upon favorable terms.

#### XVIII

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence of record, in giving effect to its letter of January 27, 1959, to Transit, and to other ex parte communications with the officials of Transit.

#### XIX

The Commission erred as a matter of law in said Order and Opinion, and acted arbitrarily, capriciously, unreasonably, and without and contrary to the substantial evidence or record in approving rates of fare which are unjust, unreasonable, unfair, discriminating and unlawful.

WHEREFORE, plaintiffs pray that this Court will:

(1) enter an order sustaining this appeal and vacating the Commission's Order 4631 of March 2, 1960;

(2) enjoin Transit from charging the rates of fare purportedly authorized by Order 4631 and order Transit to charge the rates of fare in effect prior to March 6, 1960; and

(3) grant such other and further relief as the Court may deem just and proper.

---

Leonard N. Bebchick  
706 A Street, S.E.  
Washington, D. C.

---

Leonard S. Goodman  
4336 River Road, N. W.  
Washington, D. C.

---

Barrington D. Parker  
1130 Sixth Street, N. W.  
Washington, D. C.

---

George Spiegel  
10831 Lorain Avenue  
Silver Spring, Maryland

\* \* \*

[Entered June 5, 1961]

UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA

LEONARD N. BEBCHICK, et al	:	
	:	
Plaintiffs	:	
	:	
v.	:	Civil Action No. 1529-60
	:	
PUBLIC UTILITIES COMMISSION	:	
OF THE DISTRICT OF COLUMBIA,	:	
et al	:	
	:	
Defendants	:	

O R D E R

This matter comes before the Court on what amounts to a joint request to the Court to reconsider its order entered March 29, 1961 wherein the Court found there were material issues of fact existing in the case, and denied the respective motions of the parties. For the reasons set out hereinafter, the Court will vacate its order entered March 29, 1961.

This is a statutory appeal from Order No. 4631 of the Public Utilities Commission of the District of Columbia issued as a result of prolonged proceedings before the Commission denominated "In the matter of petition of D. C. Transit System, Inc. for change in schedule of rates." The subject appeal was instituted with a complaint filed in this Court by certain transit riders. The substance of the complaint was that the Commission erred as a matter of law in the order appealed from and in its opinion in support thereof and that



the Commission acted arbitrarily, capriciously, unreasonably and without and contrary to the substantial evidence of record in its determination. Subsequently, plaintiffs moved for summary judgment, the Commission moved to dismiss the appeal, and hearing was held by the Court on March 6, 1961.

#### SCOPE OF REVIEW

The Court's powers as well as its duties and limitations are governed by statute (Act of March 4, 1913, 37 Stat. 989, ch. 150, Sec. 8, par. 64 to 69(a) incl. (Sec. 43-705 to 43-710, D. C. Code, 1951)). The statute provides that appeals to the District Court shall be heard upon the record before the Commission; that in the determination of any appeal from an Order of the Commission, the review by the Court shall be limited to questions of law; that the findings of fact by the Commission shall be conclusive unless it shall appear that such findings are unreasonable, arbitrary or capricious; and that upon the conclusion of its hearing, the Court shall either dismiss the appeal and affirm the Order of the Commission or sustain the appeal and vacate the Commission's order.

#### THE COURT'S REVIEW

Insofar as here pertinent, this matter first came before the Court for hearing and argument on plaintiffs' motion for summary judgment and defendant Public Utilities Commission's motion to dismiss the complaint on March 6, 1961 and again on

May 15, 1961. Upon further consideration of the pleadings; the points and authorities in support of and in opposition to the respective motions; the arguments of counsel for all parties; and the record certified on appeal, the Court concludes that the findings of the Public Utilities Commission are supported by the record; and are not unreasonable, arbitrary, or capricious. The Court further concludes that the conclusions and decision of the Public Utilities Commission are not erroneous as a matter of law, and accordingly it is, by the Court, this 5th day of June 1961,

ORDERED, that the order of the Court entered March 29, 1961 be and it is hereby vacated; and be it further

ORDERED, that the plaintiffs' motion for summary judgment be and the same is hereby denied; and be it further

ORDERED, that the defendant Public Utilities Commission's motion to dismiss be granted and Order No. 4631 of the Public Utilities Commission dated March 2, 1960 be and it is hereby affirmed.

---

LEONARD P. WALSH, Judge

\* \* \*

[Filed June 26, 1961]

UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA

---

LEONARD N. BEBCHICK, et al

Plaintiffs

vs.

PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA,  
et al

Defendants

---

Civil Action No. 1529-60

NOTICE OF APPEAL

Notice is hereby given that Leonard N. Bebchick and Leonard S. Goodman, plaintiffs above named, hereby appeal to the United States Court of Appeals for the District of Columbia Circuit from the Order of this Court entered June 5, 1961 which denied plaintiffs' Motion for Summary Judgment, granted defendant Commission's Motion to Dismiss and affirmed the Commission's Order No. 4631.

DATED: June 26, 1961

---

Leonard N. Bebchick  
1632 K Street, N. W.  
Washington 6, D. C.

---

Leonard S. Goodman  
4336 River Road, N. W.  
Washington, D. C.

**PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA  
WASHINGTON 4, D. C.**

**COMMISSIONERS**  
**GEORGE E. C. HAYES**  
CHAIRMAN  
**HAROLD A. KERTZ**  
**A. C. WELLING**  
BRIGADIER GENERAL, U.S. Army  
**NORMAN B. BELT**  
EXECUTIVE SECRETARY

January 27, 1959

**CHESTER H. GRAY**  
GENERAL COUNSEL  
**LLOYD B. HARRISON**  
COUNSEL  
**J. W. FALK**  
CHIEF ACCOUNTANT  
**JAMES G. SOMERVILLE**  
CHIEF ENGINEER

Mr. James H. Flanagan, Vice President  
and Comptroller  
D. C. Transit System, Inc.  
56th and M Streets, N. W.  
Washington 7, D. C.

JAN 27 1959

Dear Mr. Flanagan:

The receipt is acknowledged of your letter dated January 14, 1959, wherein you submit, in compliance with our letter of October 3, 1958, a program for conversion from street railway operations to bus operations to be completed in 1963. We note you advise that, while the program is tentative in some particulars, it is your plan to conform substantially to the program as outlined by you.

Section 7 of the franchise granted to your Company (Public Law 757 - 84th Congress - 2d Session) specifically provides that your Company "shall be obligated to initiate and carry out a plan of gradual conversion of its street railway operations to bus operations within 7 years" from the date of enactment of the Franchise Act. In the opinion of the Commission the conversion program outlined in your said letter of January 14, 1959, if initiated and carried out substantially in accordance with the time schedule therein described, will satisfactorily meet the congressional mandate set forth in Section 7 of the Franchise Act.

By direction of the Commission:

*Norman B. Belt*

Norman B. Belt  
Executive Secretary



**PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA  
WASHINGTON 4, D. C.**

**COMMISSIONERS**

**GEORGE E. C. HAYES**  
CHAIRMAN  
**HAROLD A. KERTZ**  
**A. C. WELLING**  
BRIGADIER GENERAL, U.S. ARMY

**NORMAN B. BELT**  
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COUNSEL  
**J. W. FALK**  
CHIEF ACCOUNTANT  
**JAMES G. SOMERVILLE**  
CHIEF ENGINEER

January 27, 1959

Mr. James H. Flanagan, Vice President  
and Comptroller  
D. C. Transit System, Inc.  
56th and M Streets, N. W.  
Washington 7, D. C.

Dear Mr. Flanagan:

The receipt is acknowledged of your letter dated January 14, 1959, wherein you request a decision by this Commission, as to when it will approve the adoption of the gross operating revenue method for the determination of the rate earned by D. C. Transit System, Inc. We construe your letter as a request for an expression of the Commission's views as to when you may reasonably anticipate the adoption of the gross operating revenue method. In reply thereto the Commission has to advise as follows:

The Commission is mindful of the legislative policy as enunciated by Congress in Section 4 of the Franchise Act that the Commission should encourage and facilitate the shifting from the system rate base to the gross operating revenue base as promptly as possible and as conditions warrant. The Commission is also mindful that good regulatory practice justifies at this time a tentative determination as to when "conditions" will warrant a changing over to the gross operating revenue method in order that the Company may formulate long range policies and plans for the time when the system rate base method may no longer be employed in the regulation of rates.

The Commission has advised you on several occasions that substantial progress in converting street railway operations to bus operations, with the related investment of additional capital for the purchase of new bus equipment to replace retired street cars, as well as abandonment of a substantial percentage of track based on mileage, would be important considerations in any determination as to when, in the opinion of the Commission, conditions would warrant changing over to the gross operating revenue method of regulating rates.

Cc: ORC, IMB, AL, MF, HMS, JGB, IBC, AES, AFS, OEP, FWCo., SOH

Mr. James H. Flanagan, page 2.

It is the considered view of the Commission that the major conditions to be met by the Company before a shifting to gross operating revenue method is warranted, would include compliance with the following:

- (1) A conversion of street railway operations to bus operations measured by abandonment of not less than 55 per cent of street railway track on the basis of mileage; or
- (2) Completion of not less than 51 per cent of the conversion program as measured on the basis of new busses purchased (or committed to be purchased) to replace retired street cars; and
- (3) Adoption of a firm program of gradually replacing existing busses which are more than 16 years of age.

The Commission desires to point out that in order for the Company to comply with condition (1) above, (miles of track abandoned) or with condition (2) above, (new busses acquired to replace street cars), the conversion program, as proposed by the Company in its separate letter of January 14, 1959, would have to be completed through Stage 4, which is scheduled to occur during the year 1960.

It should be clearly understood, however, that while adoption of the gross operating revenue method for fixing rates will entitle the Company, under the provisions of Section 9(b) of the Franchise Act, to a return of 6-1/2 per cent on gross operating revenues before there is any liability for motor vehicle fuel taxes, the Commission does not construe the provisions of Section 4 of the Franchise Act as requiring a 6-1/2 per cent return on gross operating revenues for rate-making purposes. It is the Commission's view that the final determination of the return to which the Company is entitled for rate-making purposes is an administrative function of the Commission in the rate-making process, and that it was not the intention of Congress to limit the Commission's duty and responsibility in this respect, since the return to which the Company is entitled is a matter for determination in the light of circumstances as they exist at the time, after giving full consideration to the interests of both investors and consumers under sound regulatory principles.

By direction of the Commission:

/S/ NORMAN B. BELT

Norman B. Belt  
Executive Secretary



STREETCAR TRACK ABANDONMENT

<u>Stage</u>	<u>Effective Date</u>	<u>Description</u>	<u>Bus Require- ments</u>	<u>TRACK ABANDONED</u>	
				<u>S.T.Feet</u>	<u>Percent of Total</u>
1	8/26/56	Eliminate scheduled rail operation on M Street west of Wisconsin Avenue	2	7,102	.9
2	9/7/58	Eliminate scheduled rail operation of the North Capitol Street and the Maryland car lines in their entirety.	57	166,492	22.2
3	1/3/60	Eliminate scheduled rail operation:			
		(a) Cabin John car line.			
		(b) Tenleytown - Pennsylvania Ave.			
		(c) Georgia Avenue - 7th Street car line.			
		(d) Potomac Park Loop (all lines)			
		(e) S.W. Mall Loop (all lines)	106	277,330	37.0
		Northern carhouse	-	7,259	1.0
		Sub-totals	165	458,183	61.1
4	Future	Eliminate scheduled rail operation:			
		(a) Fourteenth Street car line.			
		(b) Eleventh Street car line.			
		(c) Mt. Pleasant car line.			
		(d) U Street car line.	150	291,471	38.9
			315	749,654	100.0

After such retirement the fleet of buses will comprise 964 units,  
divided by age groups as follows

<u>Manufacturer</u>	<u>Model</u>	<u>Year Acquired</u>	<u>Number of Buses</u>	<u>Seating Capacity</u>	<u>Age in Years</u>
White	788	1938	1	40	21
White	788	1939	17	40	20
Mack	CM	1940	5	40	19
White	788	1940	52	40	19
White	788	1940	2	41	19
Mack	CM	1941	24	40	18
White	788	1941	58	40	18
White	788	1942	15	40	17
White	798	1942	119	44	17
Mack	CM	1942	75	44	17
White	798-TC	1947	50	44	12
White	798-TC	1948	49	44	11
White	1144	1949	104	44	10
White	1150-DW	1952	96	51	7
White	1150-DW	1953	50	51	6
G.M.C.	TGH3102	1953	57	31	6
A.C.F.	IC41	1957	10	37	2
G.M.C.	TGH3102	1958	17	31	1
G.M.C.	TDE4512	1958	16	45	1
G.M.C.	TDE5105	1958	67	51	1
G.M.C.	PD-4104	1959	5	37-41	-
G.M.C.	TDE5301	1959	<u>75</u>	51	-
			<u>964</u>		

STATEMENT OF UNDEPRECIATED COST OF RAIL PROPERTIES

September 30, 1959

	Original Cost	Accumulated Depreciation (Note 3)	Undepreciated Original Cost	Estimated Salvage (Note 1)
Passenger streetcar	\$ 8,508,759	\$ 5,775,707	\$2,733,052	\$255,262
Rail service equipment	147,288	110,991	36,247	2,945
Track and line	12,555,795	10,476,035	2,079,760	None-Note 2
Duct system	839,836	692,033	147,803	-
Low tension cables	1,117,070	599,374	517,696	279,268
Substation equipment	<u>426,840</u> \$23,595,538	<u>260,937</u> \$17,915,077	<u>165,903</u> \$5,680,461 -558,817	<u>21,342</u> \$558,817
Net undepreciated cost, December 31, 1959			<u>\$5,121,644</u>	

Depreciation per month, to recover net undepreciated cost over  
 future annual periods (January 1, 1960 to August 15, 1963,  
 43.5 months) as required by franchise

\$117,738.94

Note 1: Salvage credits conform to estimates made by P.U.C. Consultant,  
 J. L. Ingoldsby in property study of 1954.

Note 2: Estimated salvage credits on track and line have been availed of in  
 the development of the provision for track removal and repairing and,  
 hence, are not available as a salvage credit in this study.

Note 3: Accumulations of depreciation by classes of property have been  
 computed using the 1954 property study of J. L. Ingoldsby, P.U.C.  
 Consultant, as a starting point. Depreciation accumulations since  
 that study, net of retirements, are herein reflected.

# D. C. TRANSIT SYSTEM, INC.

## D.C. TRANSIT SYSTEM, INC. AND SUBSIDIARY COMPANY CONSOLIDATED BALANCE SHEET

Exhibit No.1

16

<u>A S S E T S</u>	August 31, 1959	September 30, 1959
<b>CURRENT ASSETS:</b>		
Cash	\$ 3,215,863.87	\$ 2,859,942.21
Accounts receivable - regular	274,714.65	241,693.40
Accounts receivable - Affiliated companies	61,080.84	65,744.33
Material and supplies - at average cost or less	753,131.53	774,507.98
Prepayments	243,287.80	241,420.56
<b>TOTAL CURRENT ASSETS</b>	<b>4,548,078.69</b>	<b>4,183,308.70</b>
<b>U.S. GOVERNMENT 2-5/8% BONDS</b>	<b>149,503.13</b>	<b>149,503.13</b>
<b>PENNSYLVANIA 3-1/4% BONDS</b>		<b>20,306.69</b>
<b>PROPERTY, PLANT AND EQUIPMENT:</b>		
Road and equipment - at original cost	48,389,272.27	48,431,864.09
Less: Accumulated depreciation	30,503,983.41	30,655,342.30
<b>Road and Equipment - Net</b>	<b>17,885,288.86</b>	<b>17,776,521.79</b>
Misc. physical property - at cost, less depreciation	364,812.67	362,821.82
<b>PROPERTY, PLANT AND EQUIPMENT - NET</b>	<b>18,250,101.53</b>	<b>18,139,343.61</b>
<b>TOTAL</b>	<b>\$22,947,683.35</b>	<b>\$22,492,462.13</b>
 <b><u>L I A B I L I T I E S</u></b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable - regular	\$ 822,187.34	\$ 813,895.70
Accounts payable - Affiliated Companies	24,854.79	59,967.08
Salaries and wages payable	675,293.62	501,214.86
Interest payable	-	-
Vacation accruals	954,618.39	948,525.21
Income taxes	781,802.81	633,002.81
Other taxes	96,112.47	45,959.09
Fare tokens outstanding	124,438.80	118,853.26
Equipment purchase obligations - due in one year	942,148.00	934,648.00
<b>TOTAL CURRENT LIABILITIES</b>	<b>4,421,456.22</b>	<b>4,056,066.01</b>
<b>EQUIPMENT PURCHASE OBLIGATIONS - Due After One Year</b>	<b>2,799,669.00</b>	<b>2,765,158.00</b>
<b>RESERVE FOR INJURIES AND DAMAGES</b>	<b>1,837,997.34</b>	<b>1,868,760.23</b>
<b>RESERVE FOR MOVING AND RELOCATING</b>	<b>325,000.00</b>	<b>325,000.00</b>
<b>RESERVE FOR TRACK REMOVAL AND REPAIRING</b>	<b>3,141,201.46</b>	<b>3,216,286.06</b>
<b>EXCESS OF NET ORIGINAL COST OF PROPERTIES RECORDED BY PREDECESSOR OWNER OVER COST TO PRESENT OWNER</b>	<b>7,194,249.30</b>	<b>7,108,090.82</b>
<b>CAPITAL STOCK AND SURPLUS:</b>		
Capital Stock - authorized 100,000 shares, \$100 par value, issued and outstanding 5,000 shares	500,000.00	500,000.00
Earned surplus	2,728,089.83	2,653,101.01
<b>TOTAL CAPITAL STOCK AND SURPLUS</b>	<b>3,228,089.83</b>	<b>3,153,101.01</b>
<b>TOTAL</b>	<b>\$22,947,683.35</b>	<b>\$22,492,462.13</b>

**SUMMARY OF ADULT FARES  
IN EFFECT IN THIRTY LARGEST UNITED STATES CITIES**

	Basic Fare Paid By Majority of Passengers		Transfer Charge	Reduced Fare on Special Midtown Shuttles, etc.	Special Fares Applicable in Some Non-Rush Periods
	Cash	Token			
1. New York	15	15	Free *	-	
2. Chicago	25	25	Free	15	
3. Philadelphia	20	19 (10 for \$1.90)	Free	10	
4. Los Angeles	20	20 ( 5 " \$1.00)	Free	-	
5. Detroit	25	22.5 ( 4 " 90c. )	5	15	
6. Baltimore	25	22.5 ( 4 " 90c. )	Free	-	
7. Cleveland	20	19 ( 5 " 95c. )	3	10	
8. St. Louis	25	22.5 ( 4 " 90c. )	Free	10	20 (A)
9. WASHINGTON					
Present	20	20 ( 5 " \$1.00)	Free	-	
Proposed	25	25	Free	-	20 (B)
10. Boston	20	20	Free	15	
11. San Francisco	15	15	Free	5	
12. Pittsburgh	25	23.75 ( 4 for 95c. )	Free	10	
13. Milwaukee	20	19.5 (10 " \$1.95)	Free	-	
14. Houston	23	21.25 ( 4 " 85c. )	Free	5	
15. Buffalo	25	20 ( 5 " \$1.00)	2	-	
16. New Orleans	7	7	Free	-	
17. Minneapolis	25	20 ( 5 " \$1.00)	Free	-	
18. Cincinnati	25	23 ( 5 " \$1.15)	2	-	
19. Seattle	20	20 ( 5 " \$1.00)	Free	10	
20. Kansas City	25	22.5 ( 2 " 45c. )	Free	10	
21. Newark	14	14	None	-	
22. Dallas	23	21.25 ( 4 " 85c. )	Free	5	
23. Indianapolis	15	15	3	-	
24. Denver	15	15	Free	5	
25. San Antonio	17	17	2	5	
26. Memphis	15	15	Free	5	
27. Oakland	25	20 ( 5 for \$1.00)	Free	-	
28. Columbus	20	17.5 ( 4 " 70c. )	Free	-	
29. Portland, Ore.	25	22.5 ( 2 " 45c. )	Free	-	
30. Louisville	20	18.75 ( 4 " 75c. )	Free**	10	

Present  
Arithmetical  
Average      20.5 19.1

Present Median  
Average      20    20

\* Free within each of the several separate transit systems serving the city, except for a 3-cent transfer charge on the system operated by Fifth Avenue Coach Lines, Inc.

\*\* Issued free only when 20-cent cash fare is paid.

(A) 9 A.M. to 3 P.M. except Sundays and holidays.

(B) All hours except 6 A.M. to 9.30 A.M. and 3.30 P.M. to 7 P.M. Monday to Friday.

**D. C. TRANSIT SYSTEM, INC.**  
**Statement of Net Operating Income**  
**Future Annual Period**  
**12 Months ending December 31, 1960**  
**(At Present Fares)**

	(1) Actual 12 Months ended 9-30-59	(2) Adjustments to Future Annual Period	(3) Adjusted Total Operations	(4) Allocation to Limousine Operations	(5) Allocation to Charter & Sightseeing Operations	(6) Applicable to Mass Transportation Operations
<b>OPERATING REVENUES:</b>						
Passenger revenues	\$ 26,473,710		\$ 26,473,710	\$	\$ 803,633	\$ 26,473,710
Charter and sightseeing	803,633		803,633		60,644	
Government contracts	166,658	-106,014	60,644	88,592		141,246
Limousine rental	88,592		88,592			93,699
Station & vehicle privileges	141,246		141,246			
Rent of plant and equipment	58,479	35,220	93,699			
Total Operating Revenues	<u>27,732,318</u>	<u>-70,794</u>	<u>27,661,524</u>	<u>88,592</u>	<u>864,277</u>	<u>26,708,655</u>
<b>OPERATING REVENUE DEDUCTIONS:</b>						
Operating expenses (Schedule 1)	23,145,366	146,657	23,292,023	102,428	874,851	22,314,744
Operating taxes:						
Income taxes	828,365	-484,933	343,432	-19,984	-50,592	414,008
Other taxes (Schedule 2)	<u>586,805</u>	<u>151,765</u>	<u>738,570</u>	<u>3,449</u>	<u>41,023</u>	<u>694,098</u>
Total Taxes	<u>1,415,170</u>	<u>-333,168</u>	<u>1,082,002</u>	<u>-16,535</u>	<u>-9,569</u>	<u>1,108,106</u>
Depreciation & Amortization:						
Depreciation (Schedule 3)	2,104,208	586,807	2,691,015	34,911	54,370	2,601,734
Amortization of acquisition						
adjustment	-1,033,904		-1,033,904		-13,633	-1,020,271
Provision for track removal						
and repaving						
Total Depreciation and	<u>1,044,196</u>		<u>1,044,196</u>			<u>1,044,196</u>
Amortization	<u>2,114,500</u>	<u>586,807</u>	<u>2,701,307</u>	<u>34,911</u>	<u>40,737</u>	<u>2,625,659</u>
Total Operating Revenue	<u>26,675,036</u>	<u>400,296</u>	<u>27,075,332</u>	<u>120,804</u>	<u>906,019</u>	<u>26,048,509</u>
Deductions	<u>\$ 1,057,282</u>	<u>\$-471,090</u>	<u>\$ 586,192</u>	<u>\$-32,212</u>	<u>\$-41,742</u>	<u>\$ 660,146</u>
<b>NET OPERATING INCOME</b>						
						\$ 16,016,810

Average Investment in Rate Base  
Property (Schedule 4)

Rate of Return Earned:  
Investment in Rate Base Property  
Gross Operating Revenues

4.12%  
2.47%



Exhibit No. 39  
Schedule 3

D. C. TRANSIT SYSTEM, INC.  
Depreciation Expenses - Future Annual Period  
12 Months ending December 31, 1960

	<u>Rail</u>	<u>Bus</u>	<u>Total</u>
Actual 12 months ended September 30, 1959 Co. Exh. No. 8-A, Schedule 3	\$ 933,569	\$ 1,170,639	\$ 2,104,208
Adjustments to Current Annual Basis:			
Depreciation on 75 buses delivered in September 1959		<u>159,526</u>	<u>159,526</u>
Current Annual Basis - Co. Exh. No. 9-A, Schedule 3	933,569	1,330,165	2,263,734
Adjustments to Future Annual Basis:			
Depreciation on 4 elongated limousines purchased for special service to New York and on Massachusetts Avenue		8,794	8,794
Depreciation on 25 buses delivered in December 1959		53,671	53,671
Depreciation on 6 small buses scheduled for delivery in January 1960		2,695	2,695
Depreciation on 100 buses scheduled for delivery in May 1960		127,633	127,633
Depreciation on 36 buses retired in November and December 1959		- 27,419	- 27,419
Depreciation on 70 buses scheduled for retirement in May 1960		- 33,593	- 33,593
Adjustment to provide for amortization of undepreciated cost of rail properties abandoned on 1-3-60, over 43.5 month period to August 15, 1963 (1)	<u>295,500</u>		<u>295,500</u>
Total	<u>295,500</u>	<u>151,781</u>	<u>427,281</u>
Future Annual Basis	\$1,229,069	\$ 1,461,946	\$ 2,691,015
Allocation to Limousine Operations		- 34,911	- 34,911
Allocation to Charter and Sightseeing Operations		- 54,370	- 54,370
Applicable to Mass Transportation Operations	<u>\$1,229,069</u>	<u>\$ 1,372,665</u>	<u>\$ 2,601,734</u>

(1) Net undepreciated cost of rail properties at December 31, 1959 - Co. Exh. No. 10-A, Schedule 3	<u>\$5,121,844</u>
Estimated amount applicable to that portion of the rail system abandoned on January 3, 1960, based on percentage of single track feet abandoned - 49.40%	<u>\$2,530,092</u>
Monthly amortization over 43.5 months to 8-15-63	\$ 58,163
Monthly amount being currently provided at existing depreciation rates - 49.40% of \$67,891	<u>33,538</u>
Additional monthly provision for amortization	<u>\$ 24,625</u>
Additional provision for amortization for the Future Annual Period (x 12)	<u>\$ 295,500</u>

D. C. TRANSIT SYSTEM, INC.  
Average Investment in Rate Base Property  
Future Annual Period  
12 Months ending December 31, 1960

	Based on Original Cost	Based on Purchase Price
1. Investment in Road and Equipment at original cost	\$ 49,818,778	\$ 49,818,778
2. Plus: Balance in Construction Work in Progress	<u>467,752</u>	<u>467,752</u>
	50,286,530	50,286,530
3. Less: Balance in Reserve for Depreciation	<u>31,476,647</u>	<u>31,476,647</u>
4. Net Investment in Road and Equipment at original cost	18,809,883	18,809,883
5. Less: Balance in Account 401.3 - Acquisition Adjustment (Credit)		<u>6,332,663</u>
6. Net Investment in Road and Equipment	18,809,883	12,477,220
7. Plus: Investment in Materials and Supplies	<u>774,508</u>	<u>774,508</u>
8. Net Investment in Road and Equipment and Materials and Supplies	19,584,391	13,251,728
9. Less: Adjustment to exclude Net Investment in property devoted to Limousine Operations:		
Investment at Original Cost	187,189	187,189
Accrued Depreciation	( 99,383)	( 99,383)
Net Adjustment	<u>87,806</u>	<u>87,806</u>
10. Net Investment in Property excluding property for Limousine Operations	19,496,585	13,163,922
11. Less: Allocation of Property to Charter and Sightseeing Operations:		
Investment at Original Cost	886,390	886,390
Less: Accrued Depreciation	( 550,543)	( 550,543)
Less: Amortization of Acquisition Adjustment		( 83,268)
Allocation of Materials and Supplies	<u>19,231</u>	<u>19,231</u>
	<u>355,078</u>	<u>271,810</u>
12. Net Investment in Rate Base Property devoted to regular passenger service	\$ <u>19,141,507</u>	\$ <u>12,892,112</u>
13. Average of Investment based on Original Cost and based on Purchase Price	\$ 16,016,810	

D. C. TRANSIT SYSTEM, INC.  
Road and Equipment in Service - Weighted  
Future Annual Period  
12 Months ending December 31, 1960

Balance per books of Road and Equipment in Service as of September 30, 1959 - Account 401.1		\$47,943,163.14
Cost of 25 new buses to be recorded in Road and Equipment in December 1959 as shown in Company's working papers	\$ 766,737.50	
Summary of Retirements to be recorded in December 1959	( 391,704.10)	<u>375,033.40</u>
Road and Equipment as of December 31, 1959		\$48,318,196.54
Cost of 6 new buses (Coachettes) to be delivered in January 1960 - \$42,000 11-1/2 months or 95.8333% x \$42,000 =	\$ 40,250.00	
Cost of 100 new buses to be delivered in May 1960 - \$3,125,700 7-1/2 months or 62.5% x \$3,125,700 =	1,953,562.50	
Cost of 70 buses to be retired in May 1960 7-1/2 months or 62.5% x \$(822,689.08)	( 514,180.67)	<u>1,479,631.83</u>
Weighted Balance of Road and Equipment in Service as of December 31, 1960		\$49,797,828.37
Road and Equipment - Leased		<u>20,949.67</u>
Road and Equipment in Service at Original Cost		<u>\$49,818,778.04</u>

CIVIL AERONAUTICS BOARD  
FORM 41 REPORTS: SCHDS P1 & P2

EXHIBIT 42  
Page 2 of 3

INCOME STATEMENT Group II and Group III Air Carriers		AIR CARRIER <u>Allegiant, Inc.</u> OPERATION PERIOD ENDED <u>June 30, 1979</u>		AIR CARRIER <u>Allegiant, Inc.</u> OPERATION PERIOD ENDED <u>June 30, 1979</u>	
		QUARTER		12 MONTHS TO DATE	
<b>OPERATING REVENUES</b>					
<b>TRANSPORT:</b>					
Passenger	3901	802,317		3,280,272	
United States mail	3902	-		-	
Foreign mail	3903	-		-	
Property	3906	85,269		285,263	
Charter	3907	52,151		648,942	
Other	3919	10		10	
Total transport revenues		941,047		4,574,387	
<b>NONTRANSPORT:</b>					
Federal subsidy	4100	-		-	
Incidental revenues (net)	4600	134,061		205,964	
Total nontransport revenues		134,061		205,964	
Total operating revenues		1,075,108		4,661,351	
<b>OPERATING EXPENSES</b>					
Flying operations	5100	369,718		1,766,732	
Maintenance	5400	196,138		859,189	
Passenger service	5500	99,121		99,305	
Aircraft and traffic servicing	6400	112,978		228,573	
Promotion and sales	6700	145,002		290,367	
General and administrative	6800	95,005		961,617	
Depreciation and amortization	7000	169,094		621,431	
Total operating expenses		1,138,156		4,828,236	
Operating profit or loss		63,028		166,025	
<b>NONOPERATING INCOME AND EXPENSE—NET</b>					
Net income before income taxes	8100	3,158,277		3,461,170	
Income taxes for current period	9100	647,284		2,646,501	
Net income before special items		2,447,475		2,679,976	
<b>SPECIAL ITEMS:</b>					
Special income credits and debits (net)	9796	-		-	
Special income tax credits and debits (net)	9797	-		-	
Net income after special items		2,447,475		2,679,976	
<b>UNAPPROPRIATED RETAINED EARNINGS:</b>					
Beginning of period	2940	679,062		1,287,725	
Dividends declared		51,853		175,409	
Retained earnings adjustments		-		702,138	
End of period (including net income)		1,070,689		1,070,689	

\*Denotes minor amounts, in no units \$100, \$700, and \$940.  
Amounts in thousands.

U. S. GOVERNMENT PRINTING OFFICE: 1969 O-328884

SCHEDULE P-1.2

SCHEDULE P-1.2

SCHEDULE P-1.2

CAB Form 41

Exhibit 42  
Page 3 of 3

NOTES TO INCOME STATEMENT	TRANS. CARRIER AIR CARRIER Airways, Inc. OPERATING PERIOD ENDED June 30, 1959
<p><b>Special Items</b></p> <p style="text-align: right;"><i>deleted auth 9-23-59</i></p> <p><del>A/C 2786 - \$3,103,903 represents net proceeds from sale of 350,000 shares of common stock of a wholly owned subsidiary (D. C. Transit) to the general public.</del></p> <p><del>A/C 2787 - \$647,784 represents estimated Federal Income tax on the stock sale proceeds.</del></p> <p>A/C 2840 - A dividend in the amount of \$55,853 was declared by the board of directors on June 15th, payable on July 15th, 1959 stockholders of record as at June 30, 1959.</p>	

COST OF EQUITY CAPITAL AND FAIR RETURN ON EQUITY  
For D. C. Transit System, Inc.

Line

1.	Indicated Earnings-price Ratio	11.16%
2.	Cost of Acquisition Allowance <sup>1/</sup>	12.76%
3.	Indicated Cost of Equity (Line 1 x 112.76%)	12.58%
4.	COST OF EQUITY CAPITAL AND FAIR RETURN ON EQUITY For D. C. Transit System, Inc.	<u>12.58%</u>

\* As corrected TR 1076-78

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<sup>1/</sup> The net proceeds from a public sale of 350,000 shares of D. C. Transit System, Inc. (Delaware) common stock in May, 1959, were \$3,103,983. The cost of acquisition was \$396,017 or 12.76 percent of the net proceeds. To account for this cost, the earnings-price ratio must be multiplied by 112.76 percent.



TRANSIT COMPANY EARNINGS-PRICE RATIOS  
1952 - 1958

	P e r c e n t							Average (Neg.=0)
	1952	1953	1954	1955	1956	1957	1958	
The Baltimore Transit Company	N.A.	20.7	6.9	8.9	1.6	11.3	7.8	9.53
Capital Transit Company	7.3	7.2	5.6	-	N.A.	N.A.	N.A.	6.70 <sup>1/</sup>
Cincinnati Transit Company	13.6	19.3	2.9	6.7	9.5	12.2	5.9	10.01
Dallas Transit Company	17.3	14.4	31.8	20.5	15.0	25.9	18.7	20.51
Fifth Ave. Coach Lines, Inc.	15.6	9.2	12.4	10.0	7.6	10.4	-	9.31
Galveston-Houston Company	13.5	10.5	10.1	10.4	9.8	8.4	10.3	10.43
Kansas City Public Service Company	26.4	27.5	12.3	7.8	1.0	-	19.0	13.43
National City Lines	15.1	14.7	12.7	11.4	10.6	12.6	6.7	11.97
Niagara Frontier Transit	27.0	31.6	4.4	17.8	3.3	9.5	-	13.37
Railway Equipment and Realty Co., Ltd.	13.6	-	13.8	1.0	1.5	12.4	4.3	6.66
St. Louis Public Service Company	8.5	9.2	5.6	4.5	5.3	6.0	7.6	6.67
Twin City Rapid Transit Company	-	10.7	7.5	6.7	7.2	7.5	1.9	5.93
United Transit Company (Del.)	<u>20.4</u>	<u>20.9</u>	<u>14.4</u>	<u>22.3</u>	<u>16.4</u>	<u>18.6</u>	<u>14.6</u>	<u>18.23</u>
Annual Average	14.86	15.07	10.80	10.67 <sup>1/</sup>	7.40	11.23	8.07	11.16 <sup>2/</sup>

Note: A dash denotes a negative figure.  
"N.A." refers to "Not Available," or in the case of Capital Transit to "Not Applicable."

<sup>1/</sup> Capital Transit's figure for 1955 is omitted because of the lengthy strike in that year.

<sup>2/</sup> Average of annual averages. The average of the individual company figures is 10.92%.

CURRENT EARNINGS-PRICE RATIO  
of D. C. Transit System, Inc.

<u>Month 1959</u>	<u>Monthly Closing Market Price <u>1/</u></u>	<u>Reported Earnings Per Share <u>2/</u></u>	<u>Earnings-price Ratio</u>
May	11.75		
June	12.25		
July	11.875		
August	13.0		
September	12.375		
October	12.5		
November	<u>11.625</u>		
Average	12.2	\$.36	3.0%

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1/ D. C. Transit System, Inc. (Delaware) common stock A, as reported on the American Stock Exchange.

2/ Reported net operating income of the Washington company of \$892,765 for the 12 months ending November 30, 1959, divided by the outstanding 2,500,000 shares of common stock of the Delaware parent.

CURRENT FIXED CHARGES COVERAGE BY EARNINGS AT RECOMMENDED EQUITY RATE

A. Current earnings requirements to service \$100 of net investment (Line B.3. plus $12.58 \times 42\frac{1}{2}\%$ or \$5.28)			\$9.05
B. Margin of safety for the debt capital			
1. Amount of debt	\$58.00 <sup>1/</sup>		
2. Current interest rate	<u>6.50%</u>		
3. Fixed interest expense			\$3.77
4. Balance remaining			
(a) After income taxes	\$5.28		
(b) Income taxes (\$11.48 - \$5.28)	<u>6.20</u>		
(c) Before income taxes (\$5.28 ÷ .46)	\$11.48		
5. Coverage of fixed interest before income taxes (\$3.77 + \$11.48) ÷ \$3.77			4.0

1/ The debt-equity ratio of D. C. Transit System, Inc. at September 30, 1959 was 58 percent debt and 42 percent equity as follows:

	<u>Amount</u>	<u>Percent of Total Invested Capital</u>
Debt Capital		
Equipment purchase obligations		
Due in one year	\$ 934,648	
Due after one year	<u>2,765,158</u>	
Total	\$3,699,806	58%
Equity Capital		
Reported earned surplus (Exh. 16)	\$2,653,101	
Adjustment (See Order 4577)	<u>481,212</u>	
As adjusted	2,171,889	
Capital stock	<u>500,000</u>	
Total	\$2,671,889	42%
Total Invested Capital	\$6,371,695	100%

Reported Net Income After Taxes of Leading Corporations  
As % Margin on Sales and % Return on Net Assets for 1958 -  
Individual Industries

No. of Cos.	Industry	Percent Margin on Sales <sup>1/</sup>	Percent Return on Net Assets <sup>2/</sup>
13	Meat Packing	0.5%	4.4%
26	Traction and Bus	1.0	4.4
35	Chain stores--food	1.4	15.2
73	Wholesale and misc.	2.0	9.5
22	Amusements	2.2	4.1
60	Department and specialty	2.5	9.1
14	Dairy products	2.6	11.8
39	Aircraft and parts	2.6	14.5
32	Restaurant and hotel	2.6	7.3
72	Textile products	2.7	4.3
46	Clothing and apparel	2.7	6.0
20	Air transport	2.7	5.9
58	Chain stores--variety, etc.	2.8	8.7
20	Brewing	3.0	7.8
24	Shoes, leather, etc.	3.0	8.7
20	Baking	3.2	11.5
81	Building, heat, plumb., equip.	3.4	7.6
21	Sugar	3.5	6.1
17	Furniture, wood products	3.5	7.4
22	Railway equipment	3.5	5.8
11	Distilling	3.6	7.0
50	Automobile parts	3.6	6.8
22	Construction	3.7	14.9
80	Misc. manufacturing	3.8	8.7
33	Household appliances	3.9	8.6
6	Mail order	3.9	10.2
48	Hardware and tools	4.0	6.2
111	Other metal products	4.0	9.1
52	Misc. transportation	4.0	9.6
24	Tires, rubber products	4.1	10.5
83	Other food products	4.2	11.4
112	Electrical equip., radio & tv.	4.2	12.2
15	Autos and trucks	4.2	8.8
44	Printing and publishing	4.3	11.4
153	Machinery	4.3	8.0
11	Agricultural implements	4.6	7.3
19	Soap, cosmetics, etc.	5.4	15.7
24	Coal mining <sup>3/</sup>	5.4	6.0
16	Tobacco products	5.7	14.6
76	Instruments, photo. goods, etc.	5.7	12.2
39	Other business services	6.0	14.7
71	Paper and allied products	6.2	9.1
26	Metal mining <sup>3/</sup>	6.2	6.5
49	Iron and steel	6.3	8.2

No. of Cos.	Industry	Percent Margin on Sales <sup>1/</sup>	Percent Return on Net Assets <sup>2/</sup>
113	Class 1 railroads <sup>4/</sup>	6.3	3.8
22	Paint and varnish	6.4	12.8
44	Nonferrous metals	6.4	6.7
26	Office equipment	6.6	14.1
26	Lumber	6.7	9.0
17	Glass products	7.1	11.9
72	Chemical products	7.2	11.1
58	Other stone, clay products	7.9	11.6
121	Petroleum prod. and refining	8.4	10.2
13	Shipping	9.2	8.0
27	Drugs and medicines	11.4	21.9
246	Electric power, gas, etc. <sup>4/</sup>	13.4	10.0
33	Telephone and telegraph <sup>4/</sup>	13.8	9.6
30	Cement	16.1	16.0
8	Other mining, quarrying <sup>3/</sup>	19.5	12.3

<sup>1/</sup> Profit margins computed for all companies publishing sales or gross income figures, which represent about nine-tenths of total number of reporting companies, excluding the finance groups; includes income from investments and other sources as well as from sales.

<sup>2/</sup> Book net assets at the beginning of each year are based upon the excess of total balance sheet assets over liabilities; the amounts at which assets are carried on the books are far below present-day values.

<sup>3/</sup> Net income is reported before depletion charges in some cases.

<sup>4/</sup> Due to the large proportion of capital investment in the form of funded debt, rate of return on total property investment would be lower than that shown on net assets only.

SOURCE: First National City Bank of New York Monthly Letter, "Business and Economic Conditions," April, 1959.

Public Petitioners  
Friendship Citizens Association

Exhibit No. 48  
Page 1 of 2

IN THE  
UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA

WILLIS J. MARTIN, ET AL.,	:	
	:	
Plaintiffs,	:	
	:	
v.	:	Civil Action No. 947-59
	:	
PUBLIC UTILITIES COM-	:	
MISSION OF THE DISTRICT	:	F I L E D
OF COLUMBIA, ET AL.,	:	
	:	May 29 1959
Defendants.	:	
	:	HARRY M. HULL, Clerk

ORDER

Upon consideration of the Motions of the defendants, Public Utilities Commission of the District of Columbia and D. C. Transit System, Inc., to dismiss the complaint in this action and the memoranda of Points and Authorities in support thereof, and the plaintiffs' Answer in Opposition to the said Commission's motion, and after oral argument of Counsel for all parties, and it appearing to the Court that the letter of the defendant, Public Utilities Commission of the District of Columbia, dated January 27, 1959, from which this appeal was taken, is not a final order or decision and therefore not subject to review, the Court concludes that the motions of the defendants to dismiss this action should be granted and that the plaintiff's Motion for Summary Judgment becomes moot. Therefore, it is by the Court, this 29th day of May, 1959,



ORDERED that the motions of the defendants, Public Utilities Commission of the District of Columbia and D. C. Transit System, Inc., to dismiss the complaint be, and they are hereby, granted, and that the plaintiffs' Motion for Summary Judgment be, and it is hereby, denied.

(SEAL)

A True Copy

Test: Nov 27 1959

Harry M. Hull, Clerk,

By /s/ Barbara E. Baldwin  
Deputy Clerk.

/s/ Alexander Holtzoff

United States Judge District Judge

DIVIDEND RECORD AND DIVIDEND YIELD  
ON PAID-IN STOCKHOLDER INVESTMENT  
Of D. C. Transit System, Inc.  
Since the Formation of the Company

Dividends<sup>1/</sup>

<u>Date Payable</u>	<u>Amount</u>
Dec. 30, 1957	\$290,000
Sept. 30, 1958	100,000
Oct. 20, 1958	100,000
Dec. 1, 1958	100,000
Dec. 31, 1958	100,000
Apr. 10, 1959	100,000
July 8, 1959	100,000
Oct. 9, 1959	125,000
Jan. 8, 1960	<u>125,000</u>
Total Dividends Paid -	<u>\$1,140,000</u>

Dividend Yield on paid-in equity investment of \$500,000:<sup>2/</sup>

Total yield thru Jan. 15, 1960	228.0%
Average annual yield (3.417 years)	66.4%

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<sup>1/</sup> Source: Transcript, pages 246-47 and 250.

<sup>2/</sup> There has been no change in the paid-in equity since the formation of the Company in 1956.

AVERAGE ANNUAL RETURN REALIZED ON STOCKHOLDERS' INVESTMENT  
D. C. Transit System, Inc.

Average equity investment:

Aug. 15, 1956 - Dec. 31, 1956	\$ 448,415
Dec. 31, 1956 - Dec. 31, 1957	511,905
Dec. 31, 1957 - June 30, 1958	705,170
June 30, 1958 - Sept 30, 1959 <sup>1/</sup>	<u>1,727,624</u>

Average equity investment (Aug. 15, 1956 - Sept 30, 1959) <sup>2/</sup>	<u>\$1,021,496</u>
--	--------------------

Total earnings through Sept. 30, 1959:

Earned surplus at Sept. 30, 1959 <sup>1/</sup>	\$2,171,889
Add: Dividends paid August 15, 1956 through September 30, 1959	<u>890,000</u>
Total earnings	<u>\$3,061,889</u>

<u>Average annual return on equity (37-1/2 mos.)</u>	<u>95.92%</u>
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<sup>1/</sup> Balances at Sept. 30, 1959, reflect adjustment,  
per PUC order 4577.

<sup>2/</sup> Average for each period has been weighed by number  
of months in each period.

ADEQUACY OF RESERVE PROVISIONS AT SEPTEMBER 30, 1959  
FOR TRACK REMOVAL, REPAVING, AND FINAL DISPOSITION OF RAIL PROPERTIES  
Of D. C. Transit System, Inc.<sup>1/</sup>

Reserve Provisions at September 30, 1959

Reserve for Track Removal and Repaving	\$ 3,216,286
Unamortized balance of original acquisition adjustment of \$10,339,041 <sup>2/</sup>	<u>7,108,091</u>
Total reserve provision on books for track removal, repaving, and final disposition of rail properties	\$10,324,377
Deduct: Undepreciated cost of rail properties at September 30, 1959 (D. C. Transit Exh. 10-A, Sch. 5)	<u>5,121,644</u>
Gross remainder available for track removal and repaving	\$ 5,202,733
Deduct: Related Federal income tax credits reflected on books of company through September 30, 1959 <sup>3/</sup>	<u>1,696,818</u>
Net remainder available on books of Company at September 30, 1959 for track removal and repaving	\$ 3,505,915
Additional net reserve accrual necessary over period Oct. 1, 1959 to Aug. 15, 1966 (82.5 months)	1,264,515
Total net reserve accrual required to provide total estimated costs of track removal and repaving	<u>\$ 4,770,430</u>

Proof of Adequacy of Above Reserve:

Gross provision for track removal and repaving	\$10,441,960
Deduct: Income tax credits of 54.3148%	<u>5,671,530</u>
Net reserve provision required	<u>\$ 4,770,430</u>

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<sup>1/</sup> Based on balance sheet at Sept. 30, 1959, Exhibit No. 16.

<sup>2/</sup> Representing purchaser's valuation adjustment of rail property book values, including assumed liability to remove tracks and repave. See p. 2, infra.

<sup>3/</sup> This adjustment reverses Federal income tax reductions entered on the books of the Company from Aug. 15, 1956 thru Sept. 30, 1959, based on deductions of \$3,263,112, or 52 percent of \$87,016.32 x 37.5 months.

EXCERPT FROM THE TESTIMONY OF  
JAMES H. FLANAGAN, VICE-PRESIDENT AND COMPTROLLER  
D. C. TRANSIT SYSTEM, INC. ON AUGUST 18, 1958  
In Application of D. C. Transit System, Inc., for a  
Change in Schedule of Rates, P.U.C. No. 3602

[Transcript page 987:]

[Witness Flanagan on direct examination:]

1       A utility company is entitled to earn a fair re-  
2       turn on the fair value of its property devoted to public  
3       service. In this jurisdiction, "fair value" is synonymous  
4       with "original cost".

5       That leads us to consideration of the difference  
6       between the net original cost of properties recorded by the  
7       predecessor owner, Capital Transit Company, over the cost  
8       to D. C. Transit System, Inc. The consideration given by  
9       D. C. Transit System, Inc. for the purchase of the proper-  
10      ties of Capital Transit Company did not consist only of  
11      cash and securities. The consideration included also the  
12      obligation, accepted by D. C. Transit System, Inc. to con-  
13      vert from streetcar operation to bus operation, to remove  
14      the streetcar tracks and to repave the track area. This  
15      obligation could be and has been measured in terms of money.

16      It was suggested to this Commission by our ac-  
17      countants, the nationally-known firm of Price Waterhouse and  
18      Company, that the difference we are discussing should be  
19      labeled as a reserve for track removal and repaving, and  
20      that the costs of such work be charged against this reserve  
21      as the work was done. . . .

INVESTED CAPITAL AT SEPTEMBER 30, 1959  
Of D. C. Transit System, Inc. 1/

Debt Obligations

Due in one year	\$ 934,648	
Due after one year	<u>2,765,158</u>	\$3,699,806

Capital Stock

(5,000 shares issued and outstanding @ \$100 par value)		500,000
---	--	---------

Earned Surplus

Reported earned surplus \$2,653,101

Debit adjustment (See Order 4577)	<u>481,212</u>	<u>2,171,889<sup>2/</sup></u>
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Total Invested Capital at September 30, 1959		<u><u>\$6,371,695</u></u>
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1/ See D. C. Transit Exhibit No. 16.

2/ Of this balance, \$1,700,151 or (\$2,181,363 - \$481,212 adj.) represents profits from the sale of properties to the D. C. Redevelopment Land Agency in January, 1959 (P.U.C. Order 4577). The Company has indicated its intention of claiming exemption from Federal income taxes on the profits from the sale of its Southwest property under the involuntary conversion provisions of the Internal Revenue Code of 1954. As an incident thereto, the proceeds from the sale of the property must be invested in replacement property by the end of 1960.



PROJECTED NET OPERATING INCOME STATEMENT  
For D. C. Transit System, Inc.  
Calendar Year 1960 - at Present Fares

Item	Mass Transportation Operations		
	P.U.C. Staff Projection <sup>1/</sup>	Adjustments	As Adjusted
Passenger revenue	\$26,473,710	\$ -	\$26,473,710
Station, vehicle, other rev.	234,945	-	234,945
Total operating revenue	\$26,708,655	\$ -	\$26,708,655
Operating expenses	22,314,744	-	22,314,744
Income taxes	414,008	589,661(F)	1,003,669
Motor Fuel Tax - D.C. (See below)	-	-	-
F.I.C.A. taxes	466,147	-41,443(E)	424,704
Other taxes	227,951	-	227,951
Depreciation - Rail	1,229,069	-1,110,195(A)	118,874
Depreciation - Bus	1,372,665	-246,253(D)	1,126,412
Amortization of acquisition adjustment	-1,020,271	1,020,271(B)	-
Provision for track removal and repaving	1,044,196	-860,267(C)	183,929
Total operating deductions	\$26,048,509	\$ 648,226	\$25,400,283
Net operating income	\$ 660,146	\$ 648,226	\$ 1,308,372
Deduct: D.C. Motor fuel tax			
Gross tax	\$365,762 <sup>2/</sup>		
Less:			
Fed. inc. tax cr.	181,024		
D.C.-Ad. inc. tax credit	17,639		
Net fuel tax			167,099
Adjusted net operating income (after D.C. motor fuel tax)			\$1,141,273

RATE OF RETURN:

- As percent of \$16,016,810 rate base projected by P.U.C. Staff (Exhibit No. 39, Schedule 4) 7.13%
- As percent of property rate base of \$12,041,217 recommended by Witness Harris for Public Petitioners and Friendship Citizens Association 9.48%
- As percent of invested capital of \$6,371,695 at September 30, 1959, as adjusted pursuant to P.U.C. Order No. 4577 17.91%

<sup>1/</sup> Exhibit No. 39.

<sup>2/</sup> For 12 months ended September 30, 1959, D. C. Transit Exhibit No. 10-A, Schedule 2.

EXPLANATION OF ADJUSTMENTS:

- (A) The position taken by the witness sponsoring this exhibit (Harris) is that the reserve provisions applicable to rail properties on the books of D.C. Transit at September 30, 1959, are adequate to cover the remaining depreciable book values of all such properties and to substantially provide for the costs of track removal and repaving (Exh. 51-A). Therefore, no allowance for further depreciation of those properties should be made after that date. The total depreciation adjustment of \$1,110,195 represents normal rail property depreciation of \$814,695 (Exh. 10-A, Sched. 4) plus amortization of \$295,500 as allowed by the FUC staff (Exh. 39, Sched. 3).
- (B) To reverse the acquisition adjustment amortization, in accordance with (A) above.
- (C) To reverse the provision of \$1,044,196 for track removal and repaving and to enter in lieu thereof a net reserve provision of \$183,929 for 1960, in accordance with Exhibit 51-A, which exhibit shows that the additional net reserve accrual required from Oct. 1, 1959 through Aug. 14, 1966 (or 82.5 months) is only \$1,264,515, or an annual net provision of \$183,929. This net provision is equivalent to a gross expense provision of \$402,601 less an income tax credit of 54.3148% or \$218,672.
- (D) To adjust bus depreciation to reflect the removal from the depreciation base of the original cost of fully-depreciated buses to be operated in 1960. Of these fully-depreciated buses, 371 with an original cost of \$4,066,344 will be used during the period Jan. 1 through Apr. 30, 1960, while 301 with an original cost of \$3,243,655 will be in use from May 1 through Dec. 31, 1960:
- |         |                         |   |                |
|---------|-------------------------|---|----------------|
| 33.333% | (\$4,066,344 x .07)     | = | \$ 94,881      |
| 66.667% | (\$3,243,655 x .07)     | = | <u>151,372</u> |
|         | Total credit adjustment |   | \$ 246,253     |
- (E) D. C. Transit's projection of FICA taxes represents an increase of 43.5% over this expense for the 12 months ended September 30, 1959, while the FUC staff projection reflects a 38.3% increase (\$345,816 to \$478,263). A 1960 estimate of \$435,728 is made herein,

based on an increase of 5% to reflect salary and wage increases, and 20% on top of that to reflect the FICA tax rate increase from 2.5% to 3%. Of this amount, \$12,116 is apportioned to charter, sightseeing and limousine operations and \$424,704 to mass transportation. The basic increase of 5% is probably high, since increases in the wages of those employees over \$4,800 will not result in additional FICA taxes.

- (F) To reflect income tax effect of above adjustments (except tax effect of track removal adjustment, which is provided in note C above):

Elimination of D.C. Transit tax deduction claim for track removal and repaving	\$1,044,196
FICA tax adjustment	41,443
Total adjustment credits	<u>\$1,085,639</u>

Additional income tax:	
D.C. (4.60%); Md. (.2225%)	52,352
Federal (52% of adjustment credit remainder)	537,309
Total additional income tax	<u>\$ 589,661</u>

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA  
Order No. 4001

May 29, 1953

IN THE MATTER OF	)	
	)	
Investigation of the Practices, Charges,	)	P. U. C. No. 3530,
and Accounting relating to Depreciation	)	Formal Case No. 427.
of CAPITAL TRANSIT COMPANY	)	

Under date of February 7, 1947, this Commission issued its Order No. 3151, prescribing for Capital Transit Company a composite annual accrual rate for depreciation of 4.9% of the original cost of depreciable property included in Road and Equipment Account 401.1, effective January 1, 1947. Accruals for depreciation since January 1, 1947, have been recorded in accordance with the provisions of that order.

A study has been recently completed by the staff of the Commission to determine what revisions, if any, should be made in the rate or rates for accruing depreciation. This study has been reviewed by the Company, and agreement has been reached on a revised schedule of annual depreciation rates by classes of property as set forth on the appendix attached hereto. At a pre-hearing conference in the above captioned proceeding on May 29, 1953, the results of the staff study and the revised schedule of depreciation rates as agreed to by the parties were presented for consideration by the Commission.

After consideration of the facts presented at the pre-hearing conference, the Commission is of the opinion that the rates proposed for the various classes of property are proper and should be adopted. Therefore,

IT IS ORDERED:

Section 1. That the rate of annual depreciation accruals provided for by Order No. 3151, effective January 1, 1947, be terminated as of June 30, 1953.

Section 2. That the revised schedule of rates of annual depreciation accruals for the various classes of property, as set forth on the appendix hereto, be, and they are hereby, prescribed for use by the Capital Transit Company effective July 1, 1953.

Section 3. That this proceeding be, and it is hereby, separated from the proceeding in Formal Case No. 424.

Section 4. That this order shall remain in effect until further order of the Commission.

A TRUE COPY:

By the Commission:

Chief Clerk

E. J. MILLIGAN  
Executive Secretary

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA  
Appendix to Order No. 4001 in Formal Case No. 427

Schedule of Rates for Annual Depreciation Accruals for  
CAPITAL TRANSIT COMPANY  
effective July 1, 1953.

Group No. (A)	Class of Property (B)	Estimated Average Service Life (Years) (C)	Estimated Average Net Salvage (Percent) (D)	Rate for Annual Depreciation Accruals (Percent) (E)
1	Buildings and Structures (General Office Buildings, Shop, Car- house and Garage Structures, Station Structures and Facilities, Miscel- laneous Structures, Substation Structures)	40.5	—	2.5
2	P.C.C. and Streamline Type Street Cars	23.0	3.0	4.2
3	Accessory Equipment for Street Cars and Buses	31.0	2.0	3.2
4	Rail Service Equipment	46.5	2.0	2.1
5	Locomotives	25.5	10.0	3.5
6	Passenger Buses	14.0	2.5	7.0
7	Track and Line (Overhead Trolley Track-Paved, Overhead Trolley Track-Unpaved, Special Work for Overhead Trolley Track, Conduit Track, Special Work for Conduit Track)	33.5	(5.6)	3.2
8	Duct System	39.0	—	2.6
9	High Tension Cable	50.0	25.0	1.5
10	Low Tension Cable	39.0	25.0	1.9
11	Substation Equipment	43.0	5.0	2.2
12	Shop, Carhouse and Garage Equipment	25.0	10.0	3.6
13	Tools and Work Equipment	20.0	5.0	4.8
14	Automotive Service Equipment	12.5	15.0	6.8
15	Communication Equipment	20.0	5.0	4.8
16	Furniture and Office Equipment	19.0	15.0	4.5

( ) = Negative Salvage

PRICE WATERHOUSE & CO.

1000 VERMONT AVENUE, N.W.

WASHINGTON 5, D.C.

October 18, 1956

To the Board of Directors  
The Universal Corporation  
(formerly Capital Transit Company)

We have examined the accompanying balance sheet of Capital Transit Company as of August 14, 1956/and the related statement of net loss and surplus for the period then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying balance sheet and related statement of net loss and surplus, as supplemented by the notes thereto, present fairly the financial position of Capital Transit Company at August 14, 1956/and the results of operations for the period January 1, 1956/to August 14, 1956/in accordance with generally accepted accounting principles consistently applied.

Price Waterhouse.



CAPITAL TRANSIT COMPANY

BALANCE SHEET

AUGUST 14, 1958 ✓

(With accompanying notes)

Current and working assets (Note 1):

Cash	\$ 7,580,650.46✓
Accounts receivable, current	99,809.86✓
Account receivable, due after 1958✓	24,000.00✓
Note receivable	20,000.00✓
U. S. Government securities - at cost	60,037.50✓
Prepaid expenses	82,014.58✓
Materials and supplies, at average cost or loss	724,013.55✓
Cash deposits in connection with sale of assets to D.C. Transit System, Inc.	582,000.00✓
Less: Contra liability account	(500,000.00)✓
	<u>8,652,525.95</u>

Liabilities (Note 1):

Accounts payable	\$ 243,575.15✓	
Salaries and wages	425,592.02✓	
Vacation accruals (Note 3)✓	112,889.35✓	
Real estate, income and other taxes	81,923.70✓	
Reserve for disputed local taxes	480,244.97✓	
Fare tokens outstanding	235,655.13✓	
Reserve for injuries and damages	<u>1,234,953.08✓</u>	
		<u>2,814,833.40✓</u>
		5,837,692.55

Not current and working assets

Property, plant and equipment - at original cost (Note 1)✓

Less: Accumulated reserve for depreciation, at rates prescribed by Public Utilities Commission	47,582,752.37✓
Reserve for extraordinary depreciation of track and roadway facilities (Note 4)✓	29,541,403.73✓
Reserve for loss on sale of assets (Note 4)✓	4,230,844.13✓
	<u>6,108,197.06✓</u>

7,702,307.45✓

13,540,000.00

Not assets

Stockholders' equity:

Capital stock - authorized and issued, 960,000 shares, \$19.50 par value	\$18,720,000.00
Capital surplus	30,000.00
Earned surplus (deficit)	(5,210,000.00)
	<u>13,540,000.00</u>

**CAPITAL TRANSIT COMPANY**  
**STATEMENT OF NET LOSS AND EARNED SURPLUS (DEFICIT)**  
**FOR THE PERIOD JANUARY 1, 1956 TO AUGUST 14, 1956**  
**(With accompanying notes)**

Operating revenue	\$15,941,321.81✓
Revenue deductions and other charges	8,344,853.15✓
Conducting transportation	1,483,074.11✓
Fuel, electric power and garage expenses	1,901,253.61✓
Maintenance of plant and equipment (Note 2)✓	757,209.48✓
Provision for injuries and damages	547,870.16✓
Employee health, insurance and retirement	838,522.17✓
Administrative and general	
Real estate, gross receipts and payroll taxes	894,206.73✓
Depreciation, including \$2,545,844.13✓	
extraordinary depreciation of track and roadway facilities (Note 4)✓	3,794,142.97✓
Non-operating income, net	(281,737.10)✓
	<u>16,279,395.28</u> ✓
	(338,073.47)✓
Net loss	

	<u>Earned surplus</u>	<u>Capital surplus</u>
Balances at beginning of period	\$ 252,745.68✓	\$ 16,700.06✓
Net loss for the period as above	(338,073.47)✓	
Refund of 1953 income taxes	1,019,298.97✓	
Transfer relating to investment in former subsidiary, Glen Echo Park Company	(13,299.94)✓	13,299.94✓
Provision for loss on advances to and investment in Montgomery Bus Lines, Inc.	(22,474.18)✓	
Provision for loss on sale of assets to D. C. Transit System, Inc. (Note 4)	(6,108,197.06)✓	
Balances at end of period	<u>(5,210,000.00)✓</u>	<u>30,000.00</u> ✓

## NOTES TO THE FINANCIAL STATEMENTS

### (1) Events after balance sheet date:

On August 15, 1956, the company sold all its assets, including cash, subject to all liabilities known and unknown, to D. C. Transit System, Inc., for the sum of \$13,540,000 consisting of cash, \$9,662,000, and notes of \$3,878,000. Such notes are secured by a first lien deed of trust on all real estate, improved and unimproved, sold to D. C. Transit. The sale followed the enactment of Public Law 757, 84th Congress (approved July 24, 1956) which granted (1) an operating franchise to D. C. Transit System, Inc. and (2) continued the corporate life of Capital Transit Company. Prior to enactment of Public Law 757, the company's charter and operating franchise had been revoked, both to be effective August 14, 1956, by Public Law 389, 84th Congress. At a special meeting on August 3, 1956 the shareholders voted to:

1. Sell the company's assets, subject to liabilities to D. C. Transit System, Inc. for the sum stated above,
2. Reincorporate the company under the District of Columbia Business Act and,
3. Change the company's name to The Universal Corporation.

Changes (2) and (3) were effected on August 16, 1956.

### (2) Maintenance costs:

Following enactment of Public Law 389 (approved on August 14, 1955), whereby the company's franchise and charter were limited to one year thereafter, the company curtailed certain maintenance activity of a long-range character that was deemed to be essential only to a period of operations extending beyond August 1956. Maintenance costs for equipment, way and structures for the six months ended June 30, 1956 amounted to \$1,547,309 as compared with \$2,174,629 in the like period in the prior year. Comparisons beyond the above six months are not

practicable, however, because of the employees' strike from July 1, 1955 through August 21, 1955 during which period the company did not operate its transportation system.

(3) Vacation accruals:

The amount of \$112,889.35 represents the accrued vacations of salaried employees only. The company discontinued accruing for vacations for hourly-rated employees as of July 1, 1955. The provision accrued to that date aggregating approximately \$634,000 related to vacations which the employees were entitled to take and which were taken during the period July 1, 1955 to August 14, 1956. Under the terms of the labor agreement dated August 21, 1955 the company had no liability to pay vacations for hourly-rated employees other than that described above.

(4) Extraordinary depreciation  
Loss on sale of assets

At the time the company's franchise and corporate charter were revoked in August 1955 and throughout the ensuing eleven months governmental and regulatory authorities of the District of Columbia expressed the intention that after the company ceased to operate, transportation in Washington would be provided exclusively by buses. As a consequence the company was faced with premature loss of useful life of its investment in track and roadway facilities and it proceeded at once to make provision for extraordinary depreciation so as to effect retirement of that portion of the investment that would not be recovered through normal depreciation charges. A total of \$4,230,844.13 was so provided by charge to expense, \$1,687,000.00 in 1955 and \$2,543,844.13 in 1956. Over and above this, the loss on the sale of the company's assets on August 14, 1956 amounted to \$8,108,197.06 provision for which was charged to earned surplus account.

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

November 27, 1957

IN THE MATTER OF

Determining The Net Operating Income  
of D. C. TRANSIT SYSTEM, INC. For The  
Twelve-Month Period Ended August 31, 1957,  
As Required Under And For The Purpose Set  
Forth In Section 9 Of Public Law No. 757

P.U.C. No. 3592

FINDINGS AND CERTIFICATION

TO THE BOARD OF COMMISSIONERS, D. C.:

Statute Involved

Under the provisions of Section 9(c) of Public Law No. 757, 84th Congress, 2d Session, granting a franchise to D. C. Transit System, Inc. and for other purposes, the Public Utilities Commission is required as soon as practicable after the 12-month period ended August 31, 1957, to make a determination of the net operating income of said D. C. Transit System, Inc. (hereinafter usually referred to as the "Company") for such 12-month period and the amount in dollars by which it exceeds or is less than a 6-1/2 per centum rate of return for such 12-month period, and to certify the results of such determination to the Commissioners of the District of Columbia or their designated agent. In compliance with this provision of the franchise, the Commission has made such a determination, the details of which are set forth hereafter with supporting exhibits.

\* \* \*

Rate Base Method Required by Statute

In Section 8 of Public Law No. 757, certain outright exemptions from the payment of taxes are granted, including exemption from the payment of the D. C. gross receipts tax. Liability for the payment of motor vehicle fuel taxes is conditioned, however, under the provisions of Section 9, upon whether or not the Company earns a 6-1/2% rate of return on the system rate base, except that with respect to any



period for which the Commission utilizes the operating ratio method of fixing rates, the 6-1/2% rate of return shall be applied to gross operating revenues. The Company has contended that under the provisions of Section 9 the Commission could and should make the determination for the 12 months ended August 31, 1957, on the operating ratio method. With operating revenues for the 12-month period amounting to approximately \$25,600,000, this would mean that the Company would be entitled to earnings of \$1,664,000 before there would be any liability for motor vehicle fuel tax. Deducting interest of approximately \$409,000, this would provide a return of 251% on the original investment of \$500,000 in equity capital. While the franchise indicates that it was the intention of Congress that the Company should be afforded the opportunity of earning a liberal return, we have an inherent responsibility to see that such return does not transcend the bounds of reasonableness. It is our belief that the change to an operating ratio method was contemplated for consideration only after the conversion program is well under way with the additional investment of capital required as an incident thereto. We have accordingly concluded, as recommended by the staff, that the determination of the Company's return for the 12 months ended August 31, 1957 must be made on the basis of the system rate base.

Under the provisions of Section 9, the Commission is free to exercise its judgment as to the amount of the rate base to which the 6-1/2% rate of return will be applied, and the amount by which net operating income exceeds or is less than a 6-1/2% rate of return, after including as an operating expense the full amount of the motor vehicle fuel tax for which the Company would be liable were it not for the provisions of this section. If the return is less than the allowed 6-1/2%, the Company is to be exempted from the motor vehicle fuel tax to the extent necessary, up to the full amount of the tax liability, to bring its return up to 6-1/2%.

#### Rate Base Determination

The conclusion that the Company's net operating income under Section 9 must be determined on the basis of a system rate base, gives rise to the question -- what is the system rate base to be used for purposes of determining the Company's liability for motor vehicle fuel tax? It is necessary to resolve this question before any determination can be made.

The Company has contended that if the operating ratio method of determining the return to which the Company is entitled is not adopted by the Commission as a basis for



its determination for the 12 months ended August 31, 1957, a system rate base of approximately \$18,000,000 based on the original cost of plant, property and equipment as recorded on the books of the predecessor company should be utilized. It has consistently maintained that both the Congress and the Commissioners of the District of Columbia during the period of negotiations for the franchise either promised or clearly indicated that such a rate base would be used for D. C. Transit. We have been advised by the Commissioners of the District of Columbia that no such promise was made by them, and we are unable to find any evidence that such a promise was made by Congress, either expressly or impliedly. The Company further supports its claim for an \$18,000,000 rate base on the fact that the excess of \$10,339,041.19 of the net original cost of property, plant and equipment as recorded on the books of the predecessor company over the purchase price to the present owner, as summarized on attached Exhibit No. 2, should be treated as a fair measure of the liability for track removal and repaving and that such liability was taken into consideration in negotiating the contract for purchase of the net assets of Capital Transit.

The staff of the Commission has recommended a system rate base of \$8,130,999 representing the average investment of the present owner in rate base property for the 12 months ended August 31, 1957, summarized as follows:

1. Average investment in road and equipment at original cost	\$47,724,645.32
2. Less average balance in reserve for depreciation	<u>30,466,428.64</u>
3. Net Investment in road and equipment at original cost	17,258,216.68
4. Less average balance in Account 401.3 - Acquisition Adjustment (Credit)	<u>9,779,009.78</u>
5. Net investment in road and equipment by present owner	7,479,206.90
6. Plus the average investment in Materials and Supplies	754,343.70
7. Less adjustment to exclude average investment in limousines for rental service	( <u>102,551.79</u> )
8. Recommended Rate Base	<u>\$ 8,130,998.81</u>

The development of the average balance for the various items shown above is set forth on Schedules 1 through 5 supporting Exhibit No. 3 attached hereto. Items 1, 2 and 6 reflect the average of the 13 monthly balances for these

items taken directly from the books of the Company. Item 4 represents the average balance of the excess of net original cost of property to predecessor owner over purchase price to the present owner in the amount of \$10,339,041.19 as of August 15, 1956, after giving effect to a recommended amortization of this amount over a 10-year period retroactive to August 15, 1956, as more fully discussed hereafter.

Item 7 above reflects an adjustment to exclude the average investment in limousines acquired for use in rental service. This adjustment is proposed by the staff on the premise that limousine rental service is not mass transportation service contemplated by the franchise. While Section 6 of the franchise authorizes the Company to engage in special charter and sightseeing service, the staff states that it has been advised that at no time was consideration given to granting a franchise for limousine rental service and that the discussion leading to the inclusion of Section 6 related to bus operations formerly rendered by Capital Transit. For this reason, the staff has proposed that the investment in limousines for rental service, as distinguished from charter and sightseeing service rendered by buses, as well as the related revenues and expenses set forth hereafter in detail, be excluded for the purpose of determining the liability for motor vehicle fuel tax. The staff reports that support for this position is found in a ruling by the Corporation Counsel, approved by the D. C. Commissioners on January 17, 1957, that the Company was liable for the payment of D. C. excise taxes in connection with the purchase of these limousines for rental service, whereas exemption is provided under the terms of the franchise in connection with the purchase of motor vehicles for use in mass transportation operations. The Commission finds and concludes that this adjustment is proper and that mass transit riders should not be burdened with losses incurred by the Company incident to its limousine rental service.

A system rate base reflecting original cost of the property to the person first devoting the property to public service, as proposed by the Company, and developed in the same manner as that heretofore set forth except for the deduction of the average balance of the acquisition adjustment in the amount of \$9,779,009.78, would amount to \$17,910,008.59. In connection with the Company proposal for the use of an original cost rate base, it has proposed that instead of treating the excess of net original cost over purchase price as an acquisition adjustment to be deducted from original cost to arrive at purchase price of the property, the amount be treated as a fair measure of the liability for track removal which the Company assumed from Capital Transit and that this amount be recorded on the books of the new company

as a reserve for track removal and repaving against which would be charged future costs for track removal and repaving as incurred without further charge against the customers. Under this proposal, the Company would be entitled to recover through depreciation the total amount of original cost of depreciable property at the annual rate of approximately \$2,000,000 per year, and at the same time would be entitled to a return of 6-1/2% on a reducing balance based on original cost to Capital Transit Company, or approximately \$18,000,000 as of August 15, 1956, with no additional charge against the customers for track removal.

Under the staff proposal of a rate base of \$8,130,999 based on purchase price of the property, the acquisition adjustment would be amortized over a 10-year period at the rate of \$1,033,904 per annum, as an offset to the depreciation charge, based on original cost, of approximately \$2,000,000 per annum, so that the net charge for depreciation based on purchase price of the property would amount to approximately \$1,000,000 per annum. The staff proposal would, however, make separate provision for the cost of track removal and repaving, estimated for purposes of this determination as \$10,441,958 by an annual charge against operations of \$1,044,196 over a 10-year period. It can be seen from the foregoing that the annual charge against income for depreciation and track removal and repaving, discussed more fully hereafter, will be approximately the same under either method. However, under the Company proposal it would be entitled to earn a return on a rate base of \$17,910,009, whereas under the staff proposal the Company would be entitled to a return on the lower rate base of \$8,130,999. A 6-1/2% return on the original cost rate base as proposed by the Company would provide a return of \$1,164,151, which after deducting interest payments of \$408,939, would leave \$755,212 available for return on equity capital, or a return of 151% on the original investment of \$500,000. A 6-1/2% return on the rate base reflecting purchase price as proposed by the staff would provide the Company with a return of \$528,515, which, after deducting interest of \$408,939, would leave \$119,576 available for return on equity capital, or a return of 23.92% on the original investment in equity capital of \$500,000.

By normal standards, the return on equity capital even at the lower level of 23.92% would appear to be more than sufficient to compensate the investors for the use of their funds. However, it is pointed out that net operating income of \$528,515 would represent a coverage of interest on debt of only 1.3 times, a highly unsatisfactory coverage from a credit standpoint for a business with much less risk than that inherent in the transit industry in general, and this

Company in particular. The Commission recognizes that this condition is the direct result of the original capitalization of the Company with debt of 93.7% and equity capital of only 6.3%, after giving effect to the payment of short-term loans in the amount of \$5,600,000. This Commission had no jurisdiction over the original capitalization of the Company. However, the Commission believes it is incumbent upon it to give due regard, as we believe was the intent of Congress, to the interests of the people of the District of Columbia and the transit riders in particular, and to endeavor to place the Company in a position of being able to raise the necessary amounts of new capital required for new equipment if the service is to be maintained at a satisfactory level. In this connection, the Company has advised the Commission of its intention to purchase 200 new buses between now and August 31, 1959, with 100 to be acquired in each year, and further that the Company has no intention of requesting any increase in fares prior to August 31, 1958.

We do not here hold that either the system rate base of \$8,130,999 recommended by the staff, or the system rate base of \$17,910,009 claimed by the Company, is a fair measure of the value of the property for purposes of our determination under Section 9. Suffice it to say that in the light of the above circumstances, and after full consideration of the proposals by the staff and by the Company, the Commission finds and concludes that the proper rate base figure to be used for purposes of determining the liability for motor vehicle fuel tax lies somewhere between the two extremes of \$8,130,999 and \$17,910,009. We recognize that the former gives no consideration to the effect, if any, on the purchase price of the assumed liability for track removal and repaving, nor to the fact that the sale was made by Capital Transit at a time when the loss of its franchise was imminent with a possibility of being required to dispose of its property in liquidation, so that the purchase price is not necessarily representative of the fair value of the property. On the other hand, in considering the Company proposal of an \$18,000,000 rate base, the Commission cannot ignore the fact that the property was acquired by the Company at substantially less than the amount at which it was carried on the books of Capital Transit Company, irrespective of the various considerations that may have entered the minds of the contracting parties in arriving at the agreed to purchase price. Moreover, the Company's claim that the assumed liability for track removal and repaving in an amount in excess of \$10,000,000 was an element of the purchase price, gives no consideration to probable future savings to be realized from track removal and repaving costs as allowable deductions for income tax purposes.

We accordingly find and conclude, without prejudice to any future rate base determination for either rate making or tax relief purposes, that a system rate base of \$13,020,503, as developed on Exhibit No. 3 attached hereto, is fair and reasonable as a basis for determining the liability of the Company for motor vehicle fuel tax under the provisions of Section 9 of the franchise. This determination gives equal weight to the original cost to Capital Transit Company and the purchase price to D. C. Transit System, Inc. A return of 6-1/2% on the rate base so determined amounts to \$846,333.

\* \* \*



**D. C. TRANSIT SYSTEM, INC.**  
**Excess of Net Original Cost of Road and Equipment as**  
**recorded on the books of Capital Transit Company at August 14, 1956**  
**over Purchase Price by D. C. Transit System, Inc.**

Purchase price per Agreement dated July 7, 1956:

Cash deposit by TCA Investing Corporation  
 applied to purchase price

\$ 500,000.00  
 9,100,000.00

Additional cash payment

First lien deed of trust, secured by all of the  
 real estate acquired by D. C. Transit System,  
 Inc., delivered to Capital Transit Company to  
 be applied against purchase price:

Per agreement \$3,940,000.00

Less cash realized from sale  
 of two parcels of land sub-  
 sequent to July 7, 1956

62,000.00

3,878,000.00

\$13,478,000.00

Total Purchase Price

Plus Liabilities Assumed:

Current Liabilities

\$ 1,099,835.35

Reserve for Injuries and Damages

1,234,953.08

Reserve for Disputed Local Taxes

480,244.97

Total Liabilities

2,814,833.40

16,292,833.40

Less Assets acquired other than net investment  
 in Road and Equipment:

Current Assets:

Cash

\$7,580,850.46

Materials and Supplies

724,013.55

Other Current Assets

201,824.44

8,506,488.45

Deferred Accounts Receivable

24,000.00

U. S. Government Bonds

60,057.50

Misc. Physical Property (Net)

2,426.59

Total Assets Acquired Other Than  
 Road and Equipment

8,592,952.54

Balance representing portion of purchase price  
 applicable to Road and Equipment

7,699,880.86

Net Original Cost of Road and Equipment as recorded  
 on books of Capital Transit Company:

Original Cost

\$47,580,148.60

Less Reserve for Depreciation

29,541,226.55

18,038,922.05

Acquisition Adjustment (Credit) Excess of Net  
 Original Cost of Road and Equipment over  
 Purchase Price

\$10,539,041.19



## D. C. TRANSIT SYSTEM, INC.

Consolidated Statement of Net Operating Income  
(Including Montgomery Bus Lines, Inc.)  
12 Months ended August 31, 1957

	<u>As Adjusted</u>
OPERATING REVENUE:	
Passenger revenue	\$ 25,053,625
Charter revenue	363,669
Government contract revenue	33,022
Station & vehicle privileges	148,558
Rent of plant & equipment	6,609
Total Operating Revenue	<u>25,605,483</u>
OPERATING REVENUE DEDUCTIONS:	
Operating Expenses:	
Maintenance of plant & equipment	3,482,925
Power	817,322
Fuel, lubricants & garage expenses	1,668,120
Conducting transportation	11,493,114
Traffic promotion	217,819
Provision for injured & damages	1,216,261
Employees' retirement & insurance	871,227
Administrative & general	1,325,104
Provision for wage increase	( 16,200)
Provision for vacations	607,000
Total Operating Expenses	<u>21,682,692</u>
Operating Taxes:	
Provision for income taxes	359,790
Provision for motor fuel taxes	375,631
Other taxes	581,307
Total Operating Taxes	<u>1,316,728</u>
Depreciation and Amortization:	
Depreciation	2,006,283
Amortization of acquisition adjustment	( 1,033,904)
Provision for track removal	1,044,196
Total Depreciation and Amortization	<u>2,016,575</u>
Total Operating Revenue Deductions	<u>25,015,995</u>
NET OPERATING INCOME	<u><u>\$ 589,488</u></u>

EXCERPTS FROM TRANSCRIPT OF HEARING  
BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA

[Page 52, line 24 - Page 56, line 4;  
Page 56, line 14 - Page 59, line 18]

By Mr. Spear:

Q Mr. Flanagan, before we go into the next question, may I ask you again to direct your attention to the question just asked, whether D. C. Transit does urge the position that the conditions in Section 4 described earlier are applicable to this proceeding and govern the determinations as to whether or not an operating ratio should be adopted?

A [Mr. Flanagan] Definitely yes.

Q Mr. Flanagan, do you have any other reasons that in your opinion, or that of the company, justify the operating ratio method? A Yes. I was giving my remarks in support of my assent to your question, Mr. Spear. In order to keep the record clear I will start again. Although this matter has been presented to the Commission on several occasions and has been reviewed by the Commission, I feel that at this time the Company is in a much stronger position than ever before to urge the shifting to the gross operating revenue base.

MR. GOODMAN: Excuse me, sir. I must object again. I feel that the witness is going beyond his competence in testifying with respect to the operating ratio as a rate-making method before this Commission. He has testified that he is Vice President, Comptroller and Treasurer of a company, but

he has not testified as to any particular competence with respect to a sound rate-making method as an economist, as a statistician, as an accountant.

CHAIRMAN HAYES: Do you want to qualify him?

MR. SPEAR: I will be glad to qualify him. Mr. Chairman. I think counsel for some of the intervenors is new to these proceedings and hasn't had the experience that we have all had.

By Mr. Spear:

Q Mr. Flanagan, prior to coming with the Company would you explain the experience you have had with regulatory matters?

MR. RICHEY: On behalf of the other intervenors, let me suggest a situation on Mr. Flanagan's qualifications as an expert witness. We all know he has been a member of the Commission and has been on the staff of the company. I think he is well qualified.

MR. SPEAR: May I have the record show that, Mr. Chairman?

CHAIRMAN HAYES: I think the Commission would probably take administrative notice of it, as a matter of fact, but since the issue has been raised I cannot deny you the right to qualify him.

By Mr. Spear:

Q Mr. Flanagan, would you state your experience in regulatory matters, both in connection with the PUC and the SEC, in a few words?

A Just prior to joining Capital Transit Company on March 1, 1953, I had completed a term of 11 years as Chairman of the Public Utilities Commission of the District of Columbia. Prior to my joining this Commission in February 1942, I had had seven years' experience, most of it as Chief Analyst of a group in the Public Utilities Section of the Securities and Exchange Commission, which group was charged with the duties of analyzing the financial setup and operations of all the holding companies and their subsidiaries within the particular group with which I was associated.

Q And then in 1953 you joined Capital Transit Company as a Vice President? A As a vice president. Soon thereafter I became the Comptroller of Capital Transit Company and in 1957 I also assumed the title of Treasurer.

Q And from 1953 to the present date you have been either with Capital Transit Company or its successor, D. C. Transit System? A Yes, in that position I have testified before this Commission several times on rate matters.

Q And have you also testified, sir, before other regulatory agencies of the local and federal governments?

A I have testified on several occasions before the Maryland Public Service Commission and on several other occasions before the Interstate Commerce Commission.

MR. SPEAR: Mr. Chairman, I believe that the witness has been established as an expert witness and I would move that his testimony be accepted as opinion evidence.

MR. GOODMAN: The objection is withdrawn in view of the witness's testimony.

\* \* \*

THE WITNESS: In addition to my other remarks, I also feel that the Commission has ample reason to find that present conditions warrant such a shift. Therefore, for the purposes of this record, I desire to review the history of what has happened to date relating to this very important subject. When it granted a franchise to D. C. Transit System, Inc. through Public Law 757, Congress inserted the following provision in the law.

Mr. Chairman, there I quote Section 4 which is rather lengthy. It has been given before by Mr. Spear and if you care to I would be glad to read it. I think it is well for counsel to know just what Congress said in its entirety.

CHAIRMAN HAYES: You can present it in the manner in which you see fit, Mr. Flanagan. Of course we know what Section 4 says. We have read it lots of times.

THE WITNESS: There may be some at the table who haven't read it carefully.

"Section 4. It is hereby declared as a matter of legislative policy that in order to assure the Washington Metropolitan Area of an adequate transportation system operating as a private enterprise, the corporation, in accordance with standards and rules prescribed by the Commission, should be afforded the opportunity of earning such return as to make the corporation an attractive investment to private investors. As an incident thereto the

Congress finds that the opportunity to earn a return of at least 6-1/2 per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on either the system rate base or on gross operating revenues would not be unreasonable, and that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible and as conditions warrant; and if conditions warrant not later than August 15, 1958. It is further declared as a matter of legislative policy that if the corporation does provide the Washington Metropolitan Area with a good public transportation system, with reasonable rates, the Congress will maintain a continuing interest in the welfare of the corporation and its investors."

Another provision in Public Law 757 which is pertinent to this discussion is Section 7, which reads as follows:

"Section 7. The corporation shall be obligated to initiate and carry out a plan of gradual conversion of its street railway operations to bus operations within seven years from the date of the enactment of this Act upon terms and conditions prescribed by the Commission, with such regard as is reasonably possible when appropriate to the highway development plans of



the District of Columbia and the economies implicit in coordinating the corporation's track removal program with such plans; except that upon good and sufficient cause shown the Commission may in its discretion extend beyond seven years, the period for carrying out such conversion."

Although we have always been of the opinion that the provisions of Section 4 and Section 7 should not be considered as having a strong bearing upon each other, we recognize that the Commission and its staff has tied in these two sections and have considered them as being interdependent. Accordingly, when the company converted its North Capitol Street and Maryland streetcar lines, and this conversion affected over 20 per cent of the total single track footage, we contended that substantial compliance had been had with the provisions of Section 7, and that the Commission should find that conditions warranted the shift to the gross operating revenue base as contemplated in Section 4. However, the Commission found in its Order Number 4480, dated August 28, 1958, that conditions at that time did not warrant shifting to such gross operating revenue base method. Several discussions and conferences followed. On January 14, 1959, the company presented to the Commission a statement showing the contemplated stages of conversion of the entire streetcar system to bus operations.

[Page 61, Line 20 - Page 62, Line 25]

By Mr. Spear:

Q Mr. Flanagan, would you continue your discussion of these letters?

A [Mr. Flanagan] In the first letter, Exhibit Number 4, the Commission expressed the opinion that the conversion outlined in the company letter dated January 14, 1959, if initiated and carried out substantially in accordance with the time schedule therein described, will satisfactorily meet the congressional mandate set forth in Section 7 of the Franchise Act. In its second letter of January 27, 1959, Exhibit 5, the Commission expressed the considered view that the major conditions to be met by the company before a shifting to gross operating revenue method is warranted, would include compliance with --

MR. GOODMAN: I object to this hearsay on the one hand.

CHAIRMAN HAYES: Hearsay? MR. GOODMAN: Yes.

CHAIRMAN HAYES: I don't follow you. What do you mean, hearsay?

MR. GOODMAN: The gentleman is testifying as to a letter from a Mr. Belt and as to a position of the Commission that Mr. Belt represents. This, I take it, is hearsay.

MR. SPEAR: I don't believe, Mr. Chairman, that it comes under any known definition of hearsay.

CHAIRMAN HAYES: I am a little disturbed. I don't know what there is about it that would be hearsay. Here is a letter to which this gentleman representing the company testifies that the company received as a communication addressed to him and coming from our Executive Secretary. How could that be hearsay? I will overrule the objection.

[Page 63, Line 1 - Page 66, Line 9; Page 66, Line 20 - Page 74, Line 9; Page 74, Line 22- Page 77, Line 6]

By Mr. Spear:

Q You were describing the second letter, Exhibit Number 5, Mr. Flanagan.

A [Mr. Flanagan] Yes. The major conditions to be met are

(1) A conversion of street railway operations to bus operations measured by abandonment of not less than 55 per cent of street railway track on the basis of mileage; or

(2) Completion of not less than 51 per cent of the conversion program as measured on the basis of new buses purchased, or committed to be purchased, to replace retired streetcars; and

(3) Adoption of a firm program of gradually replacing existing buses which are more than 16 years of age.

Q Would you please discuss each of the conditions enumerated by the Commission in its letter of January 27, 1959, Exhibit 5, and explain the manner in which the company is meeting these conditions?

A Yes, and in order to facilitate an understanding of my remarks I have prepared an exhibit which may be helpful to the Commission.

Q Mr. Flanagan, I have in my hand a one-page exhibit entitled "Streetcar Track Abandonment." Is this the exhibit to which you have just referred? A Yes, sir.

MR. SPEAR: Mr. Chairman, I ask that this exhibit be marked for identification as Petitioner's Exhibit Number 6.

\* \* \*

By Mr. Spear:

Q Would you proceed, Mr. Flanagan, with your discussion of Exhibit Number 6?

A First, let us examine the condition that not less than 55 per cent of street railway tracks be abandoned through conversion to bus operations. The data on Exhibit 6 has been prepared to cover the period from August 15, 1956. The exhibit describes the conversion from streetcars to buses by stages. All abandonments of streetcar track have resulted from conversion to bus operations. There will be some departures from the schedule submitted to the Commission on January 14, 1959, as it was anticipated there might be. I shall endeavor to explain the differences.

As of August 15, 1956, there were 749,654 single track feet of streetcar tracks in operation. As this exhibit shows, 173,594 feet have already been abandoned through the conversions explained in Stages 1 and 2.

CHAIRMAN HAYES: That is the additions of 1 and 2, I take it?

THE WITNESS: Yes. An additional 284,598 feet will be abandoned as of January 3, 1960. The conversion described in Stage 2 represents a substantial change from that originally contemplated and will hasten the completion of conversion. The aggregate number of feet abandoned and to be abandoned at this time or on January 3rd, 1960, namely, 458,183 feet, represents 61.1 per cent of the total single track feet in operation on August 15, 1956, which indicates compliance with the first provision contained in the Commission's letter dated January 27, 1959. Please understand that no track is considered abandoned because one line is discontinued, if such track is still to be used by other lines. As an example, I might state that Stage Number 2 contemplates the substitution of buses, on the Number 30 streetcar line, from Friendship Heights to Barney Circle. However, the tracks in the vicinity of Barney Circle will still be used by, I believe, the New Jersey Avenue car line. Therefore, that track is not considered as being abandoned.

COMMISSIONER KERTZ: Is that the only example that you have?

THE WITNESS: Wherever tracks are used by more than one car line, Mr. Commissioner. It is planned that one of the two or three lines will continue to use that trackage. It is not then considered to be abandoned trackage.

By Mr. Spear:

Q Then do I understand that on January 3, 1960, there will be 61.1 per cent of abandonment of single track footage in operation on August 15, 1956, exclusive of, or over and above, that trackage which may still be used by another line and therefore not considered as abandoned? Is that correct?

A That is correct.

■ \* \*

By Mr. Spear:

Q Mr. Flanagan, will you now discuss the condition stated by the Commission relative to the completion of not less than 51 per cent of the conversion program as measured on the basis of new buses purchased, or committed to be purchased, to replace retired streetcars?

A As this exhibit shows -- Exhibit Number 6 -- it is calculated that the maximum number of buses to be required to provide service in substitution for the rail service to be abandoned will be 315.

That is less than the 359 figure which I submitted to this Commission back in January. I have questioned our operating people closely as to the difference. There is a representative of the company who is more familiar with all of the details than I am, but I am assured that the 315 stipulated as the bus requirement as of this date will meet conditions as of this date. Of course, the Public Utilities



Commission has control over the service to be substituted for the streetcar lines, so there is protection in that direction. However, during the year 1959 rearrangements of service, improvements in rendition of service, have made it possible to give equivalent service with a smaller number of buses than was contemplated at the beginning of the year.

CHAIRMAN HAYES: What you are saying, sir, if I understand you correctly, is that whereas in your letter to us dated January 14 you indicated that it would take 359 buses to replace the streetcars, that your reshuffle indicates to you that it can be done with 315?

THE WITNESS: That is correct, yes, sir.

By Mr. Spear:

Q Mr. Flanagan, of those 315 buses, have they been described and are they included in one of the columns on Exhibit Number 6?

A Yes, under bus requirements we indicate the number of buses which have replaced streetcar service in Stages 1 and 2 and the number of buses which will go into service on January 3, 1960, to replace the streetcar operations described under Stage 3.

Q Now, Mr. Flanagan, would you relate the bus requirements for the 51 per cent conversion requirement of the Commission's letter of January 27, 1959, Exhibit 5? Would you relate that to the number required as shown on your Exhibit Number 6 and tell us how many of these you have purchased or are committed to purchase?

A New buses purchased, or committed to be purchased, aggregate 300. Of these new buses, 100 were received in the fall of 1958; 75 were received in September 1959; 25 are expected before the end of 1959; and 100 which are on order are scheduled for delivery in the spring of 1960. As of this date we have complied with the PUC condition to the extent of acquiring 55.5 per cent of the maximum number of buses required to replace streetcars; when the additional 25 buses are received, the compliance will be to the extent of 63.5 per cent; and when the 100 buses now on order are received the compliance will be to the extent of 95.2 per cent.

Q Mr. Flanagan, do I understand, then, that by the end of 1959, by which time you expect to have the additional 25 buses, you will have complied with the conversion program to the extent measured by new buses to the extent of 63.5 per cent? A That is correct. Substantial retirements of old buses occurred during the year 1958. These retirements included:

Number of Buses	Make	Year Acquired
1	Twin Coach	1938
3	Twin Coach	1939
4	Twin Coach	1939
9	Mack	1940
10	Twin Coach	1940
2	Mack	1941
19	Twin Coach	1941
1	White	1949
<u>1</u>	White	1952
50		

Q Would you describe the actual retirements during 1959, Mr. Flanagan?

A	Number of buses	Make	Year Acquired
	4	Mack	1940
	2	Mack	1941
	1	White	1941

There are presently 36 buses not required for regular operations which the company plans to retire in November 1959. These buses are described as follows:

Number of buses	Make	Year Acquired
4	Mack CM 40	1940
32	Mack CM 40-44	1941-42

Q Mr. Flanagan, do you have available the information on the fleet of buses that will remain after the retirements just described that you plan to take place in November of 1959?

A Yes, I have prepared a statement and I think it will help matters if we introduce it as an exhibit.

MR. SPEAR: Rather than have it introduced as an exhibit, Mr. Chairman, since it is not independently so prepared with a heading and all, may it be incorporated in the transcript of the testimony as if read, all parties having received a copy? It is the table of such retirements consisting of about 20 items.

CHAIRMAN HAYES: Is there any reason for not marking it for identification as an exhibit, the mere fact that it doesn't have a technical heading?

MR. SPEAR: Then I suggest it be marked as Exhibit Number 7. We did not prepare it that way but there is no reason why it cannot be so marked. I request that it be marked as Exhibit Number 7.

CHAIRMAN HAYES: It may be so marked.

(The tabulation referred to was marked for identification as Petitioner's Exhibit 7.)

THE WITNESS: This exhibit lists 964 buses divided by age groups and also identified by manufacturer, the model, the year acquired and the seating capacity.

By Mr. Spear:

Q Mr. Flanagan, would you describe the relationship of the information you have just given on the status of the fleet of buses to the conversion requirement and the conditions described by the Commission in their correspondence?

A The foregoing facts also furnish the basis for indicating that the other condition stated by the Commission is already being fulfilled. That condition relates to the adoption of a firm program of gradually replacing existing buses which are more than 16 years of age. To the extent that the new buses purchased are not immediately required to replace streetcars, we consider them as replacements for the older buses. The fact that the older buses are not immediately retired does not alter this situation in our opinion. The new buses purchased or committed to be

purchased, 300, exceed the number required for replacement of streetcars through the stages scheduled for completion immediately by 135.

In other words, referring to Schedule 6, it will be seen that 165 buses are required to replace the streetcar service already planned and we have purchased or committed ourselves to purchase 300. It is the intention of the company to acquire a minimum of 100 buses each year for at least three years, with the view to eliminating the necessity for operating buses which are too old to function efficiently. In our opinion, this represents a definite and constructive program for bus replacement, and certainly it is in full compliance with the condition contained in the Commission's letter which refers to this point.

CHAIRMAN HAYES: May I interrupt you, Mr. Flanagan? In our letter of January 27, in the third item, we say "adoption of a firm program of gradually replacing existing buses which are more than 16 years of age." Do I understand you to say that even though you have a bus and you continue to use it, that you consider it a replacement because there is a new one bought?

THE WITNESS: Not in continuous use, Mr. Chairman.

CHAIRMAN HAYES: But I say continuing to use it.

THE WITNESS: As a standby it will not be contrary to the interests of the Commission, in my opinion.

CHAIRMAN HAYES: That is your position, that even though you continue to use it that you consider that in compliance with the suggestion of replacement?

THE WITNESS: I don't mean by that continuing to use it in daily service, but I think a standby fleet of a modest amount is a wise policy. In other words, I wouldn't want to be committed that as soon as we buy a new bus we retire an old bus. The old bus may still be servicable.

CHAIRMAN HAYES: Is it your suggestion that this is compliance, which I understand you to say you are doing with respect to three, that it is a compliance where a bus is continued to be used for whatever purpose you suggest, not continuously but as a standby; that when you buy a new bus that that can be considered as a replacement even though it is still continued to be in use?

THE WITNESS: No, I do not go that far because our program is so well in advance of the condition laid down by the Commission that I don't have to take that particular position. All I am saying is that if we do not immediately retire an old bus by reason of buying a new bus, we are still in compliance with your requirement that we replace old equipment with new equipment. I do not intend that the old equipment would continue to be used in daily operation after we get the new buses. It wouldn't make good sense economically to begin with, because the economies are so much greater in the operation of new buses. That is what I am trying to imply. Maybe I haven't given you a full answer to



your question.

CHAIRMAN HAYES: I think perhaps you have. I further understand you to say that whereas your schedule shows 165 you have gotten 300, so you say you have enough leeway between those that the question of replacement would be no problem, that this would still be substantial replacement.

THE WITNESS: I say we are ahead of the game right now and we will continue to stay ahead.

\* \* \*

THE WITNESS: The over-all approach to the problem of replacing the older buses is indicated by a tabulation which shows that during 1960 we will buy -- and we are already committed -- 100 new buses. With spares and so forth we will require 60, which will leave 40 buses, to my mind, in fulfillment of your condition that we avail ourselves of new equipment to replace old.

By Mr. Spear:

Q Mr. Flanagan, when you say 60 buses, do you mean 60 buses to replace streetcars being converted?

A Yes. Part of the data which I didn't put on this particular statement also indicates definite retirement of buses indicated for each of the years 1960, 1961 and 1962. My information indicates that in 1960 we will have 40 buses to replace older buses. In 1961 we will have 37 new buses

to replace older buses, and in 1962 we will have 48 for that purpose. I haven't gone beyond 1962 because that is the period we are trying to cover in our presentation here today.

Q Mr. Flanagan, again to make certain I understand you, do you say that the 40 buses you have in 1960 left over from the 100 buses purchased will be new buses for replacement of older buses?

A That is right.

Q And the 37 that you will have in 1961 for replacement will be new buses left over from the 100 purchased to replace older buses?

A That is correct.

Q And the 48 that you referred to in 1962 will be new buses to be left over after conversion to be used for replacing older buses?

A That is correct. As a matter of fact, again, if we revert to Exhibit 6, the indication is that to completely eliminate rail operation through Stage 4 we will need 150 buses. The three years that I have enumerated here provide 175 buses for that purpose, which is ample leeway, certainly more than ordinarily is considered as necessary for spares. That to me is further indication that our program for continuing purchase of new buses will enable us to comply very well with the Commission's desires and with the company's desires, for that matter, to get rid of the old equipment gradually.

Q Do I understand correctly when you say 150, Mr. Flanagan, referring to Exhibit 6, you mean that you will need 150 new buses for the fourth stage?

A That is what I thought I said, yes.

Q In the years and the period commencing January 3, 1960, and thereafter, and the testimony you have just given as to the excess available for replacing older buses, you have actually allocated not just the 150 out of the 300 new ones but you have allocated 175 out of the 300 new ones?

A That is right.

Q And you say you will have a hundred and twenty-five of the new fleet to be purchased in the next three years available to replace older buses?

A As a matter of fact, allowing for the usual 10 per cent spares, all we need to provide in the next three years is 165 new buses to replace streetcar service for the fourth stage instead of 175. So it is a conservative estimate.

[Page 96, Line 4 - Page 99, Line 21]

Q [By Mr. Spear] Mr. Flanagan, will you explain how you arrived at the amount of depreciation shown on Exhibit Number 10 and in Line 11, I believe?

A [Mr. Flanagan] This item is of the utmost importance and requires a considerable amount of discussion. Due to the provisions of our franchise contained in Public Law 757, and in conformity with the repeated urgings of the Public Utilities Commission, we have proceeded with the conversion

from streetcar operations to bus operations. As we have already pointed out, one phase of this conversion was completed in 1958 and further substantial conversion is contemplated to be completed almost immediately.

Testimony has already been introduced in this record to show that over 60 per cent of the single track feet of rails will be abandoned. This calls for full realization of the fact that the character of the investment of the company in transit facilities has changed. It calls for an evaluation of the tremendous loss of property value that has already been realized. It calls for plans to provide for the recovery of that portion of the investment in property purchased for the purpose of devoting it to public service, which has not already been recovered through provisions for depreciation.

Schedule 4 attached to this Exhibit Number 10 shows on Page 1 the computation of the amount of additional annual depreciation, \$654,358, necessary to comply with requirements that the original cost investment in property devoted to public service should be recouped through provisions for depreciation.

Q Mr. Flanagan, when you talk of Schedule 4, I don't believe the notation "Schedule 4" is on the page to which you refer. Are you referring to the next to the last page of Exhibit Number 10?

A Yes. The last two pages attached to Exhibit Number 10

are considered to be and should be marked Exhibit Number 4.

Q Schedule Number 4.

A Schedule Number 4.

Q And those are the pages that start "Statement of Depreciation at Current, Existing Rates, September 30, 1959"?

A That is right.

Q And the second statement is entitled "Statement of Undepreciated Cost of Rail Properties, September 30, 1959"?

A Yes.

Q All right. Will you continue your explanation?

A Page 2 of Schedule 4 shows how the depreciation provision necessary to recover the net undepreciated cost of rail property over future annual periods was calculated. In the first column of this page, there is shown the original cost of streetcars and other rail property which will be abandoned as conversion to bus service takes place. As required by the company's franchise, total conversion must be accomplished by August 15th, 1963. I call attention to the amount reflected in that first column. We are in the process of abandoning property which at its original cost was \$23,595,539. The second column shows the amount of depreciation which has been accumulated through the years to provide for the recovery of the original cost of the rail property. These calculations are predicated upon a depreciation study prepared in 1954 by Mr. J. L. Ingoldsby, a member of the engineering staff of the Public Utilities Commission, and

brought up to date to September 30, 1959 by us. From that column, it will be noted that the amount accumulated is only \$17,711,404. The third column shows that there remains a balance of \$5,884,134 of the original cost which has not been depreciated, and for which provision must now be made. After providing for the estimated salvage value of all this property, or \$558,817, we arrive at the amount of \$5,325,317 as the net undepreciated cost of rail property as of September 30, 1959.

There remains 43-1/2 months from January 1, 1960 of the period of seven years stipulated in the company's franchise as the period within which conversion must be completed. The company has provided in its projections of future operations for the recovery of the net undepreciated cost of \$5,325,317 over this period of 43-1/2 months. The result is a monthly charge to depreciation of \$122,421, or an annual charge of \$1,469,053. The establishment of a provision as explained above will, of course, necessitate the discontinuance of the regular annual provision for depreciation on the property which is to be abandoned. As shown on Page 1 of Schedule 4, this annual provision amounts to \$814,695. Thus, the additional depreciation becomes the difference between the two figures, or \$654,358. Normal depreciation on buses and other property will continue as at present.



[Page 194, Line 5 - Page 197, Line 3]

Q [By Mr. Spear] Mr. Flanagan, have you examined the various exhibits marked for identification on the subject of operating ratio and made a further study of the subject matter between the date of the last hearing and this proceeding?

A [Mr. Flanagan] I have examined them, and I have formulated my own opinion as to the merits of the gross operating ratio method of determining the fare.

Q And have you prior to the proceeding and over the years that your prior testimony indicated that you were a member of this Commission and also an official of D. C. Transit and its predecessors also studied the subject of operating ratio and system rate base?

A Yes. My interest in it goes back to that first report that was offered for identification, Exhibit Number 20. I attended the convention at which the report was rendered. I discussed it with the authors of the report, and it has been very much in my mind ever since that time.

Q At the time Exhibit Number 20 was prepared were you a member of this Commission and Chairman of the Commission?

A Yes; I was.

Q Mr. Flanagan, would you please state for the record the reasons why D. C. Transit believes that the operating ratio method of determining its rate of return is appropriate

and necessary in this proceeding, quite apart from the matters relating to its franchise that were discussed at the last hearing?

A Well, a quick perusal of these exhibits and any consideration of the method that we have, upon which we have based our application, is becoming more and more recognized. Apparently regulatory commissions have become aware of the fact that it is not the size of the investment that is important, but, rather, the size of the income. This is true particularly with regard to the transit industry, which is subject to a great deal more competition than an electric, gas or telephone utility, for example.

I know there has been objection to applying the gross operating ratio method of determining rates to a combined street railway and bus company. However, we have certainly demonstrated in this proceeding that after January 3rd, 1960 D. C. Transit System, Incorporated cannot be considered a street railway company. Whatever streetcar service remains in operation after that date will exist only until the time is propitious for its conversion to bus operation. Investments in rail property have already ceased. All investments at present and in the future will relate to bus property, the life of which is very much shorter than is the case with rail property. While the investment in buses will be less than would be required for rail property, the maintenance expenses will be high as will the depreciation

charges, and those are factors which are used in determining that the adoption of the gross ratio method is necessary and desirable, I am sure, by these other commissioners and would be in my case, too.

A very important point which should be emphasized is that, due to the comparatively short life of motor vehicle equipment, which is now to be the primary investment in the industry, in the District of Columbia, certainly, the depreciated original cost rate base very often fluctuates considerably, depending upon the age of the equipment. In contrast, in the case of other utilities, with a high plant investment in relation to revenue, the depreciated rate base fluctuates little from year to year, except due to the growth factor.

Now, the possible fluctuations in the property account of D. C. Transit System, Inc. within the next few years, commencing with the elimination of the railway property, as proposed in the record now being made before this Commission, should be very apparent to all. That is another very important consideration which should guide the Commission in its adoption of the gross operating ratio method, in my opinion.

[Page 243, Line 20 - Page 247, Line 14]

Q [By Mr. Donnelly] Refer now to the liabilities section of the balance sheet, Mr. Flanagan, with particular reference

to the item for equipment purchase obligations due in one year in the amount of \$934,648.

A [Mr. Flanagan] Yes, sir.

Q And the same item due after one year in the amount of \$2,565,158, or a total of \$3,699,806. A Yes.

Q It is a fact, is it not, that as of September 30, 1959, these equipment purchase obligations represent the only indebtedness of the company outstanding?

A That is right.

Q And it is also a fact, is it not, that since August 15, 1956, and excluding for this purpose the \$5,600,000 of short-term borrowings that were paid off from the cash assets acquired from Capital Transit Company within a very short period, the company has been able to pay off \$3,878,000 of notes payable, secured by a lien on its real property, and, in addition, has paid off \$3,500,000 of notes payable secured by a chattel mortgage on the company's rolling stock?

A Yes. The first item you mentioned, as you know, was paid off principally from the proceeds of the sale of our southwest maintenance base, on which we received over \$3,200,000.

Q Can you state in a general way the principal sources of funds for the payment of the other obligations?

A Well, of course, there was cash in the company from the date of its acquisition and also cash generated through provisions for depreciation, net income.

Q And the provision for track removal and repaving, would that be another source?

A Yes. I consider that as part of the entire depreciation picture, Mr. Donnellia.

Q Referring now to the item of capital stock in the amount of \$500,000, this represents, does it not, the total investment in equity capital by TCA Investing Corporation, whose name has subsequently been changed to D. C. Transit System, Inc.? Did I say the total original investment? That is what I meant to say.

A The total original investment in equity stock; that is correct.

Q Will you give a breakdown for the record of the item of earned surplus as between that portion that is represented by the net income retained by the business and that portion represented by reported profits on the sale of your southwest property?

A Yes, sir. The figure which I have will not correspond exactly because we were requested to prepare these figures on a company-only basis and the earned surplus of \$2,653,101.01 includes the earned surplus deficit of Montgomery Bus Lines, so there will be a difference. I am referring to an earned surplus at September 30, 1959, of \$2,689,714.43. Of that amount, \$2,251,217.19 represents the profit derived from the sale of our bus maintenance base in southwest Washington to the D. C. Redevelopment Land Agency. The balance represents retained earnings.

Q Would you give me that balance, because my figures do not -- I don't have the Maryland Bus Line figures.

A The balance representing retained earnings is \$438,496.45.

Q Referring now, Mr. Flanagan, to the item of retained earnings, this amount is after declaration of dividends for the period from August 15, 1956 through September 30, 1959; is that not correct?

A Yes.

Q What are the dividend declarations since the company began operations? I would like to have them by the years, if you will.

A Dividend Number 1, payable December 30, 1957, \$290,000.

Dividend Number 2, payable September 30, 1958, \$100,000.

Dividend Number 3, payable October 20, 1958, \$100,000.

Dividend Number 4, payable December 1, 1958, \$100,000.

Dividend Number 5, payable December 31, 1958, \$100,000.

Q Making a total of \$400,000 for the year 1958?

A For the year 1958.

Dividend Number 6, payable April 10, 1959, \$100,000.



Dividend Number 7, payable July 8, 1959, \$100,000.

Dividend Number 8, payable September 30, 1959,  
\$125,000.

Dividend Number 9, payable October 9, 1959, \$125,000.

This makes a total of \$450,000 for the year 1959.

Q Could I get one detail           A Yes.

Q That last dividend, Number 9, payable October 9,  
\$125,000, when was that declared, sir?

A September 30, 1959.

Q And the total for the year was \$450,000; is that  
correct?

[Page 250, Line 4 - Line 20]

[Mr. Flanagan] If I may correct the record at this time,  
I am sure that for the year 1959 the dividend that I  
reported as Number 8 should be eliminated, in the amount of  
\$125,000. That will give us three dividends in 1959, to  
make the record perfectly clear, one payable April 10, 1959,  
for \$100,000. There is one payable July 8, 1959, for  
\$100,000. There is one payable October 9, 1959, for \$125,000.

By Mr. Donnella:

Q Or a total of \$325,000?           A Yes.

MR. SPEAR: That is right. That is what it should  
have been.

By Mr. Donnella:

Q Up to the present time, Mr. Flanagan, have there been  
any other small dividends declared?

A Yes. A dividend declared on December 7, 1959, payable January 8, 1960, in the amount of \$125,000.

[Page 326, Line 14 - Page 331, Line 3]

Q [Mr. Donnell] You know, Mr. Flanagan, that bus depreciations accrues at the present time at 7 per cent per annum on the basis of a 14-year service life, with an allowance of 2-1/2 per cent for salvage?

A [Mr. Flanagan] Yes.

Q I believe we discussed that yesterday.

A. That is in accordance with the Public Utilities Commission orders.

Q You are also familiar with the fact, are you not, that as of September the 30th, as shown on your Exhibit 7, there were 368 buses which you stated were to be retired in November, which were more than 14 years of age?

A That's what the exhibit shows; yes.

Q Under our present depreciation procedure, it is a fact, isn't it, that on the basis of 7 per cent per annum after a bus reaches the average service life of 14 years you are then accruing more depreciation than is required to meet the retirement loss based on the original cost of the bus?

A As I explained yesterday, that is necessary under the composite arrangement that's been in effect for many years, with the full knowledge and consent and direction of this Commission.

Q I am not questioning that.

A Well, I just wanted to make that clear.

Q Have you made any study of the amount of depreciation that has been accrued in excess of the original cost on these 404 over-aged buses as of September 30th?

A No; I don't have that.

Q Will you accept, subject to check, that based on a study by the Commission's staff that through September the 30th accruals in excess of \$1,200,000 have been provided over and above the requirements to meet the retirement of the original cost of these old buses?

A Subject to check, I'll take that figure.

Q And it is a fact, also, Mr. Flanagan, that this excess depreciation will continue to accumulate under present procedures so long as any of these old buses are retained in service?

A I'm accepting those figures. I don't regard them as significant, in view of the method in which we have been providing depreciation over the years.

Q Would you agree that these excess accruals on over-aged buses are available for meeting the extraordinary retirement losses that will be incurred in connection with the abandonment of rail facilities for which you have proposed an adjustment?

A Not in those terms; no. I think the -- may I give you an explanation?

Q Certainly, under what terms, if not in those terms?

A I think we have to regard the actual situation over the years with regard to our depreciation reserve and consider it in the light of the fact that it has been on the composite basis. I have put in exhibits here and testimony relating to specific rail property, which, through no decision of our own, except acceptance of a franchise, must now be abandoned, and I have testified that complete abandonment will take place by the middle of 1963. I further testified that under the depreciation system we have not recovered a very substantial portion of the original investment in that rail property and that, under all the rules of law and the courts, we are entitled to recover that portion of our original cost through provision of special amortization, by whatever means this Commission may devise, so that I do not regard whatever figure you arrive at for buses, particularly in view of the history of this reserve over the last seven or eight years, as being available to reduce what I consider to be the unrecovered cost of the rail property at this time.

I do not agree with that for one moment.

MR. DONNELLA: Would the Commission indulge me for just one moment?

By Mr. Donnell:

Q Assuming, and, of course, we have assumed, subject to check, that the figure I have given you of \$1,200,000 of excess accruals on these over-age buses has taken place, what

would be your suggestion, Mr. Flanagan, as to the use of the excess in the depreciation account for those buses?

A I think that is a part of our total reserve, which, in our opinion, is representative of the provisions which have been accumulated over the years on our entire property. I cannot consider that, in effect, our reserve on other than rail property is excessive. I don't agree with that for one moment --

Q Well --

A -- that over-all reserves are excessive. I don't agree with that.

Q I don't want you to understand, Mr. Flanagan, that I am saying there will be no retirement loss. What I have indicated to you is that there is some excess in this particular phase of the depreciation accrual, which should be used as a counter balance, shall we say, to the losses which will be realized from the early retirement of other property.

A I consider that --

Q And isn't that in effect just what you told me when you said it should be used as an over-all basis?

A It is an equalizer in the composite reserve. That's what it is.

Q Which would make it follow, would it not, that it could be used for the retirement --

A No. No.

Q I don't know what you mean by an equalizer, then.

A It is to equalize what might be deficiencies in other phases of it, but certainly not this rail property.

Q Why exclude the rail property, Mr. Flanagan?

A Because this is a definitive abandonment caused by Government regulation, and we can separate that, and when we're all through -- and the depreciation study, I am sure, will show that -- getting rid of that streetcar abandonment, there will still be a lot of streetcar property left after the rail abandonment is excluded, so that when we are all through, whatever may be placed against the buses will be just about enough, enough to offset the deficiencies in the reserve for the other property.

That's the basis on which I won't accept that.

[Page 426, Line 8 - Page 427, Line 2; Page 427, Line 21 - Page 428, Line 5]

By Mr. Spiegel.

Q Mr. Flanagan, calling your attention to Exhibit Number 13, on the first page you show an estimate for the future annual period, a rate of return of 3.5 per cent under the proposed fare structure. Do you consider that that rate of return is one that is fair to the riders, fair to the public and fair to the company?

A [Mr. Flanagan] It is fair to the riding public. It is not fair to the company.

Q What is the basis for the statement that you consider the 3.5 per cent a fair rate of return to the public?



A On the very face of it, they are not paying an excessive rate of fare for the service that is rendered.

Q What criteria do you apply? What specific criteria do you apply to reach that conclusion?

A We apply the provision in the franchise granted to us by Congress, among other things, which indicates that if we are able to earn a return of 6-1/2 per cent on our gross operating revenues, that rate of return will not be considered unfair.

\* \* \*

A Very obviously, the nature of the investment of the company is undergoing a very drastic change. It will not be long before it is a 100 per cent bus operation. Under those conditions, the continuation of the method up until now employed, basing the return on the base or the property base, would be a very dangerous system to follow as I am sure it would provide an inadequate return to enable the company to pursue its policy of replacing old equipment with new equipment and giving the riding public the best possible service in vehicles.

[Page 430, Line 9 - Page 432, Line 1]

THE WITNESS: [Mr. Flanagan] To summarize that consumer angle, to me there is only one criterion which is multiple in its nature, and that is that the company must furnish adequate service at fair, reasonable and undiscriminatory rates and if the only return it gets is 3-1/2 per cent,

that is prima facie evidence to me that those rates are on the low side of any such requirement as I have cited.

By Mr. Spiegel:

Q In other words, I am seeking specific criteria that could be used to demonstrate that 3-1/2 per cent is fair while three per cent is not fair, or four per cent is fair. In other words, where do you get 3.5 per cent? Does that come out of the air or is there some kind of calculation as is ordinarily made in public utility cases where the fairness and justness of a rate of return are demonstrated in terms of specific facts and figures which people can deal with and not generalizations?

A [Mr. Flanagan] I answered your question which was specific and related to 3-1/2 per cent. When you bring in what other commissions have done, my answer is that they have allowed a much larger rate of return than 3-1/2 per cent. I am not relating my answer to three, three and a quarter or four. You asked about 3-1/2 per cent. I said because of its low character it is extremely fair or would be extremely fair to the riding public.

Q Can you state for me any basic and specific criteria that can be applied to this rate method which is presented here by which the Commission can demonstrate that either 3-1/2 per cent or some other specific rate of return in per cent is a fair rate?

A Yes. I will just refer you to the service that is running on the streets at this very moment. That is all I need to say.

Q That is as much as you can say?

A That is all I need to say.

Q I am asking you is that all you can say.

A That is all I care to say. Any time I say any more you object.

MR. SPIEGEL: My question, Mr. Chairman, is whether that is all he can say.

THE WITNESS: No, but that is all I am going to say. That is my answer to your question.

[Page 433, Line 13 - Page 435, Line 9]

Q [By Mr. Spiegel] I would like to call your attention, Mr. Flanagan, to Page 59 of the transcript of the first day's proceedings where there is discussion of the fact that Order Number 4480 on August 28, 1958, shows that the Commission determined that conditions did not warrant shifting to the gross operating base method. In the next paragraph, beginning on Line 15, you state that several discussions and conferences followed. Can you tell me with whom these discussions and conferences were held?

MR SPEAR: Mr. Chairman, these questions were asked this morning, I believe.

MR. SPIEGEL: May I reply to that objection? I discussed this point with Mr. Goodman and Mr. Goodman asked generally about the discussions and conferences but he did not call his attention to this Page 59. I am going beyond his cross examination and it is not repetitive.

MR. SPEAR: I submit it is duplicative, Mr. Chairman, but I suppose the answer is the same, if it will expedite it.

CHAIRMAN HAYES: Let's hear the answer. We will allow the question.

MR. SPIEGEL: Thank you, your Honor.

THE WITNESS: [Mr. Flanagan] These discussions and conferences were held with members of the Public Utilities Commission.

By Mr. Spiegel:

Q Where were these conferences held?

A In the District Building.

Q In the Offices of the Commission? A Yes.

Q How many discussions and conferences were held?

A. I don't remember.

Q Who represented the company at these conferences?

A I did, generally.

Q All the members of the Commission were there?

A Not always.

Q Can you state in summary or as you may wish what the substance of these discussions and conferences was?

A Generally, the discussions and conferences culminated in the written correspondence that we received from the Commission.

Q Was any notice given to the public of these discussions and conferences? A Pardon me?

Q Was there any notice to the public of these discussions and conferences? A No.

[Page 458, Lines 1-24]

Q [By Mr. Spear] Mr. Flanagan, you were asked yesterday and today the amount of cash invested in equity stock of D. C. Transit in Washington made at its inception by the then T.C.A. Investing Corporation, now the D. C. Transit of Delaware. I believe you indicated that the cash investment was \$500,000 for stock issued. Is that correct?

A [Mr. Flanagan] Yes.

Q At the same time, D. C. Transit of the District of Columbia did or did not incur any obligations at the time it accepted this franchise?

A Very definitely upon the acceptance of the franchise from the Congress the company took on the liability for removal of track and the repaving of the track area. This estimated cost has already been testified to as running, according to one appraisal, up to \$12 million. We are recording it on our books with a liability to set up a reserve of about \$10 million. That reserve is to be created out of our current earnings year by year.

Q Is that the account that appears on Exhibit 16 as of September 30, 1959, in the amount of \$7,108,090.82 under the title of "Excess of Net Original Cost of Properties Recorded by Predecessor Owner Over Cost of Present Owner"?

Is that a reflection of other obligations assumed by D. C. Transit?

A In a sense it is, yes.

[Page 468, Line 25 - Page 469, Line 22]

MR. SPEAR: I would then like to offer in evidence Exhibits 2, 3, 4, and 5, Mr. Chairman, which relate to the exchange of correspondence in January of 1959 about which there has been quite a bit of discussion and cross-examination. I move the admission of Exhibits 2, 3, 4, and 5.

MR. DONNELLA: I have no objection to the admission of those documents.

MR. SPIEGEL: I believe I would object to them on the grounds that I don't believe they are evidence and that if they purport to be a determination by the Commission they were not made on the basis of notice to the public, with public hearings, evidence and findings, and on the ground that the Commission addressed to me a letter subsequent to its letter of January 27 in which the Commission stated that this was not their final action or determination, and on the ground that the question of these letters was taken to court and the case was dismissed on the grounds stated by Judge Holtzoff that this was not a final action or determination by the Commission.

I say these letters have no legal standing as evidence and should not be admitted. I think, if anything, the existence of these letters hurts rather than helps the D. C. Transit's case.

CHAIRMAN HAYES: We will admit them.



[Page 483, Line 24 - Page 484, Line 11]

THE WITNESS: [Mr. Flanagan] I won't give it in the complete detail. I will give you what I have right here. As of September 30, 1959, the total balance in banks was \$2,575,309, of which \$1,487,158 was in the New York banks and the balance was in Washington banks. Among the New York banks, the principal depositories, checking accounts, are Chase Manhattan Bank, Federation National Bank and First National City Bank.

By Mr. Leeman:

Q Mr. Flanagan, are all of those checking accounts which are not drawing interest?

A They are all checking accounts which are not drawing interest.

[Page 571, Line 4 - Page 572, Line 21]

A [Mr. Roberts] One condition that distinguishes D. C. Transit System from the company in Rhode Island and from many other companies to which the operating-ratio theory has been applied is that D. C. Transit still has a substantial investment in street railway plant and equipment, which includes, in addition to its passenger vehicles, such items as tracks, underground conduits, switches, car barns and yards, and electric power facilities. The November 1952 report of the Special Committee of the National Association of Railroad

and Utilities Commissioners is limited entirely to bus companies. I find no reference in this report indicating that it is applicable to companies operating a combination of streetcars and buses. The report pertains exclusively to "the use of operating ratio in fixing bus fares", and one of the conclusions of the report is that:

"The adoption of the operating ratio is not a panacea for all of the financial ills of the motor bus industry."

If I were to follow the same procedure that I did in Rhode Island, I would not recommend that the operating ratio be considered for D. C. Transit System until it was a 100 per cent bus operation. Another consideration is the relatively stable condition of employment in the District of Columbia as compared to a depressed industrial area like Rhode Island. Regard should also be given to any other special conditions, such as the reasonableness of the depreciation accruals included in operating expenses, the amount of any amortization charges that may be included in operating expenses or the amount of operating equipment that is rented rather than owned and the amount of operating rents included in operating expenses for such items as leased vehicles, machine tools and office machines.

Finally, due regard should be given to the per cent that would be earned on the company's rate base under any specific operating ratio. As a matter of fact, when

the rate base is definitely established, as it is in the case of this company, any given rate of return on the rate base is equivalent to one and only one specific operating ratio. The two factors, per cent of return and operating ratio, are absolutely tied together mathematically.

[Page 578, Line 14 - Page 579, Line 21]

Q [Mr. Donnelly] Mr. Roberts, what conclusions have you reached as a result of your studies and analyses that you have described in your testimony today and the exhibits that you have presented?

A [Mr. Roberts] My first general conclusion is that a fare structure of 25 cents cash with five tokens sold for one dollar would produce sufficient additional revenue for the company to meet its operating expenses in 1960 as computed by Mr. Falk in exhibits prepared and to be presented by him in this proceeding, with sufficient net operating income remaining to provide a fair and reasonable return on the company's investment in rate-base property.

Second, that such a fare structure is practical from the operating standpoint and has substantial advantages over the novel and temporary type of fare structure proposed by the company.

Third, with respect to the choice between the system-rate-base method and the GOR or gross-operating-revenue method of determining the return the company is entitled to earn after all taxes, a 6.5 per cent return

on the system-rate base is equivalent not to a 6.5 per cent return or commission on gross-operating revenue, but to a return of 3.5 to four percent on gross operating revenue for a so-called operating ratio of 96 to 96.5 per cent.

And, finally, that the determination of fares in the District of Columbia by use of the operating-ratio theory or GOR method will, as the report of the Special Committee of the National Association of Railroad and Utilities Commissioners pointed out, "depend, to a large extent, upon the imagination and the research activities of" this Commission, and the regard it must give to the conditions prevailing in each case.

[Page 631, Line 14 - Page 633, Line 18]

Q [Mr. Donnelly] In your opinion does a return of \$1,143,249 constitute a fair rate of return for D. C. Transit?

A [Mr. Falk] In my opinion, it does. It would enable the Company to meet its charges for interest in the estimated amount of \$317,000 on its outstanding debt capital for the year 1960; it will enable the Company to pay dividends at the present, and in my opinion liberal, level of \$500,000 per annum; it will enable the Company to absorb below-the-line charges for the twelve months ended September 30, 1959 in the net amount of approximately \$26,000 after giving consideration to the effect of income taxes thereon, and would still provide approximately \$300,000 to be retained in the business available for meeting a portion of the Company's

capital requirements or for meeting interest requirements should the Company step up its program for acquiring new buses.

Based on the investment in equity capital as of September 30, 1959 of \$3,153,101, as shown by Exhibit No. 16, in the proceeding, net income available for return on equity capital of approximately \$800,000, or \$500,000 for dividends and \$300,000 for retained earnings, would represent a return on equity capital of 25.37%. In this connection, it is pointed out that the Commission has issued its Order No. 4577 requiring the Company to reduce earned surplus in the net amount of \$481,212 in connection with claimed profits on the sale of the Company's Southwest Shop and Carhouse properties, which were credited to earned surplus. This order of the Commission is presently in litigation before the Courts. Giving effect to the reduction in earned surplus in the net amount of \$481,212 required by the Commission, the adjusted investment in equity capital would be \$2,671,889 and the return on equity capital would be increased to approximately 29.94%. In my opinion, a return on equity capital for D. C. Transit at either 25.37% or 29.94% is not excessive, when consideration is given to the relatively low per cent of equity capital invested in the business and to the risk factor inherent in the transit industry as a whole.

I would like to make it clear that my recommendation of a return at this level does not contemplate that the higher earnings will be used as a basis for another increase in the level of dividends during the ensuing year, but rather is recommended for the purpose of providing a cushion at least to some extent, for increased costs that will become effective next November 1st and thereby either eliminate or postpone the necessity for another increase in fares beyond March 1, 1961. Whether the calculation is made under the rate base-rate of return method or under the operating revenue method, it is my opinion that a return of \$1,143,249 meets the requirements of a fair rate of return and is sufficient to enable the Company to attract additional capital, to protect the financial stability of the Company and retain a portion of earnings in the business, and further that it represents a balancing of customer and investor interests.

[Page 714, Line 17 - Page 715, Line 23]

By Mr. Goodman:

Q Mr. Roberts, in your opinion, I take it you believe that operating ratio is a form of cost-plus, since, in effect, it allows a return on expenses?

A [Mr. Roberts] Yes; that is right.

Q And that there are no standards available to determine a reasonable or proper operating ratio?

A Well, one standard that is available is to consider the rate of return at the same time you consider what the



operating ratio . should be.

Q Yes. So, is it your opinion that the standard for operating ratio should be rate of return?

A I consider that is one of the most important factors to consider in determining an operating ratio when the amount of the rate base is available to the Commission.

Q And cost of capital, in turn, provides a reasonable standard for return on investment, does it not?

A Yes; that is an important factor.

Q Then, for the purposes of an earnings requirement, operating ratio is superfluous, is it not, for you obtain the cost of capital and the rate of return and, therefore get your earnings requirement for the company, do you not?

A Well, it is primarily a shortcut method and avoids having to bring the rate base up right to the last dollar every time you have a rate case.

Q Well, your operating ratio has to be related to the return, in any event, does it not? A Yes.

Q Rate of return? A Yes.

[Page 717, Lines 1 - 21]

#### REDIRECT EXAMINATION

By Mr. Donnellia:

Q Mr. Roberts, in response to a question which I understood to be: Does not the operating ratio have to be related to the rate of return? -- Did you understand a question was asked you in that vein?

A [Mr. Roberts] I had in mind in answering that in my testimony that mathematically the two are tied together; inextricably and if you know the rate base that there is only one operating ratio that will fit in with any given rate of return, and vice versa.

Q But, by the same token, is it not true, Mr. Roberts, that in the abstract proposition of operating ratio the true test is to relate it to the operating revenue, without regard to the rate of return; in the abstract?

A Yes; that is right. The operating ratio means that a certain specified number of cents are to be left over from each dollar of revenue after paying all operating expenses and taxes.

[Page 718, Line 2 - Page 721, Line 2]

By Mr. Goodman:

Q Mr. Roberts, I understand now that you adopt your counsel's characterization that the true test of operating ratio is to relate something to revenues. Isn't the test of the standard for operating ratio the underlying rate of return and the cost of capital that that rate of return demands?

A [Mr. Roberts] The one underlying test of the reasonableness of any operating ratio is the rate of return which must necessarily accompany it. As I also said, the determination of an operating ratio must take into account all the particular conditions of the specific transit system that you are dealing with.

Q There is no standard, though, for a proper or reasonable operating-ratio number for any particular company, is there?

A Well, if other things are unchanging and it is found that this company should have an operating ratio of, let us say, 96, just for the purpose of illustration, and there are no material changes in these surrounding conditions during the coming year, the fares could be set a year hence on that same standard of a 96 per cent operating ratio, without having to bring the rate base right up to date in order to make that determination.

Q How would you know the 96 per cent operating ratio would be a reasonable figure, though -- in the abstract, without relating it to a fair return on investment?

A You know it when it is determined in the first instance, right now, for example, that it should be 96 in the light of the rate-base information that we have before us, and I say if there are no changes, such as a big fleet of new buses coming in, or the company going through a sale and lease-back of its garages, or something like that, you know that a year hence the 96 operating ratio would be a reasonable and shortcut method of establishing fares a year hence. in view of whatever changes in operating expenses had taken place in that year.

Q Then are you saying the rate of return should be set now so that it can be used as a standard for operating ratio in the future?

A No; I'm not saying that. The rate of return can change due to a higher cost of money, for example, as has taken place within the last year.

Q Then I return to my earlier question of what standards you have for gauging the reasonableness of the 96 per cent operating ratio for the future period if you are not going to relate it to the rate of return.

A I have made clear that it does have an absolute relation to the rate of return when you know the rate base.

Q Therefore, the determination of the Commission in that future period would be that the resulting rate of return would also be reasonable, if the 96 per cent --

A Well, all changes that take place in that period should be considered, but if there are no material changes you can still continue with the 96 per cent operating ratio and know that it will lead to the establishment of reasonable fares.

Q Then if there are no material changes you can continue with the rate of return that was originally found to premise the 96 per cent operating ratio, could you not?

A Yes. I am assuming that during the interval the general cost of money would also be remaining the same.

\* \* \*

COMMISSIONER KERTZ: I would like to ask a question.  
Mr. Roberts, I gather from some of your testimony

that whether or not an operating ratio is reasonable is dependent in large measure upon judgment as applied to a particular company. Am I correct?

THE WITNESS: That is exactly right. Judgment based on all the circumstances of that particular company.

[Page 729, Line 24 - Page 731, Line 2]

Q [By Mr. Spear] Mr. Roberts, if it is difficult to use a system rate base for an all-bus operation because of the many factors we have discussed earlier today, would it not be even more difficult to use system rate base for a system that is in the throes of converting where it has some street railways, but where it has a large percentage of buses? Would not that complicated picture of part buses and part street railway make it even more difficult to use system rate base than the old bus system?

A [Mr. Roberts] Well, I testified in my direct that I considered the operating ratio method applicable primarily to systems that were 100 per cent bus. I stated that as a general principle. I know there is a rate base being found currently on this property. It has moved up from \$13 million to \$16 million just between this case and the last determination of the Commission relating to fuel taxes a few months ago and, in my opinion, it is still feasible to use the rate base method here until this company begins a stabilized, hundred per-cent bus operation, if it is the Commission's

judgment that that is the more desirable method to pursue. In other words, what I am saying is there is no absolute point reached in a transition from streetcar and bus to all-bus where the operation ratio method suddenly becomes the more desirable one, but when you do get to the hundred-per-cent figure you have reached a point where there are definite advantages in the operating ratio method, from the standpoint of simplification, of rate making and fair dealing with the owners of the property.

[Page 758, Line 22 - Page 760, Line 3]

Q [By Mr. Bebachick] In your personal opinion, Mr. Falk is not a purchase price valuation of the rate base the proper method to employ in this proceeding?

A [Mr. Falk] I so testified in a previous case, but the Commission has ruled three times that this is the proper procedure and I respect the decision of the Commission and have proposed this method in this case.

Q I see. But, aside from following their precedent, since you are qualified as an expert on this matter, I am trying to elicit whether your personal opinion remains the same as it was in the previous proceeding.

A My personal opinion still remains the same; yes.

Q Therefore, as far as your personal opinion goes, the proper rate base in this proceeding would be the figure \$12,892,112, in the second column on Schedule 4 here?

A That would be the rate based on purchase price; yes.



Q Do you feel that the purchase price rate base gives consideration to the effect, if any, upon the purchase price in 1956 of the assumed liability by the company of the track removal and repaving? Is that reflected in the purchase price?

A I think that was an element that was taken into consideration in the price that was paid for this company; yes.

Q So, to a degree, the purchase price reflects that assumed liability?

A I think it is as low as it is by reason of that liability, that the company was willing to sell the company at the figure it did because it was faced with that liability for track removal.

[Page 768, Line 11 - Page 769, Line 11]

[By Mr. Bebachick] Going back to Schedule 3 again, you have the net undepreciated cost of rail properties at December 31, '59, listed at a little over five million dollars. Is that correct?

A [By Mr. Falk] That is right.

Q That is reflected, is it not, in the current rate base on Schedule 4? A That is right.

Q If that whole amount is reflected and if half of that amount, which is yet undepreciated, because this whole amount, five million dollars, is an undepreciated amount, then half of that amount, that \$2,500,000, is also reflected

in the rate base. If the larger figure is, then a portion of it has to be.

A I will agree, but I say you can't take it out of the top figure and reduce the eighteen-million-dollar figure on Line 4.

Q No one is taking anything out. It hasn't been taken out for the time being. It is in there. For the time being the rate base reflects a two-and-a-half-million-dollar undepreciated figure of rail properties. A That is correct.

Q Which are abandoned right now.

A That is correct, yes, sir; but the company hasn't recovered that cost and that is why I am recommending the adjustment I do, to recover that cost.

[Page 774, Line 16 - Page 775, Line 23]

Q [By Mr. Bebachick] Back on Schedule 4, Sheet 1, the rate base computation, Mr. Falk, let's go down to Line 3, the balance in reserve for depreciation. Does that balance indicated here of some thirty-one and a half million dollars reflect a credit of \$613,661 as was ordered by this Commission in Order 4577 in connection with the gain realized on the sale to the Redevelopment Authority of properties by the company?

A [Mr. Falk] No, sir, that transfer from surplus to depreciation reserve has not been made. That matter is in litigation.

Q May I inquire why it was not made, for what reason you did not make it?

A I say the matter is in litigation.

Q Well, but the Commission has ordered this as an appropriate credit, has it not? A That is correct.

Q And since this is the Commission's feeling, should not your accountants reflect this until the courts indicate that the Commission is wrong?

A I didn't make the adjustment. I suppose there is argument for making it. I say the matter is still in litigation and until it is decided I didn't make the adjustment.

Q In view of the record of this Commission in court, do you not think it would have been proper to make that credit in your personal opinion?

A I think the adjustment was proper. I think it would not have been improper to make that adjustment.

Q That has a fairly --

A As I say, the matter is still pending.

Q And this was your reason? A Yes, sir.

[Page 848, Lines 7-22]

By Mr. Goodman:

Q Now, Mr. Falk, if the Commission adopts the rate base that you, in your personal expert opinion, believe should be adopted, the rate base based on purchase price of \$12,892,112, would a fare increase still be wanted?

A [Mr. Falk] I believe so, Mr. Goodman, because I think you look at the end result of the requirements of the

company to meet interest on debt, pay reasonable dividends and have something left over for surplus, which is a measure of a fair rate of return. Now, you could use a lower rate base, but then you would have to have a higher rate of return to produce that same amount of return, and if that return is required, by the same token you could use a higher rate base with a lower rate of return and come up with the same amount of return.

[Page 852, Line 7 - Page 854, Line 18]

Q [Mr. Goodman] And what studies regarding the level of dividends needed by this company to attract private investors have you made?

A [Mr. Falk] I have made studies that these dividends -- that the return we are allowing the company provides the company with what, in my opinion, is a reasonable return on equity capital when you take into consideration the thin equity that's involved in the capitalization of this company.

Q Have you made any study of pay-out ratios of this company or any other transit company?

A I have figures on pay-out ratios for this company and other companies.

Q Did you analyze these figures? A No, sir.

Q And compare them with other transit companies?

A No, sir; I did not.

Q Did you make any studies of dividend price ratios of this company --

A I don't think dividend price ratios with respect to transit companies mean a thing, Mr. Goodman. They bounce all over the place. You can make that kind of a study with respect to an electric company or a gas company where there are standards you can be guided by, but in the transit industry they just don't apply.

Q Then you have made no such study? A No, sir.

Q Have you made any other study of dividends needed by this company: A Of what?

Q Of dividends needed by this company to attract private investors.

A The money has been invested by private investors in accordance with the granting of the franchise, and the franchise says that they shall be allowed to earn a return that will make it an attractive investment for private investors, and I think that the dividends, while they may be on the liberal side, meet that requirement of what is an attractive investment for private investors.

Q Five hundred thousand dollars of dividends on the present company's equity investment is needed to attract private investors? Is that your testimony?

A Well, I say it is an attractive investment for a private investor, but I question whether you could go out and raise additional equity capital to put in this company. I think the additional financing will have to come from a debt capital, except to the extent that the present

investors allow earnings to remain in the business and build up your equity in that way, and that's what's happening.

Q What standards do you have for determining the reasonableness, the necessity, of the company's paying out \$500,000 in order to attract private capital? Is this just your opinion? What basis do you have?

A It is my judgment that the return on equity capital, which I have referred to, of 25 per cent, when you consider all the elements involved in the capitalization of this company, is a reasonable return for a transit company; also, when you consider the risks that are inherent in the transit operation.

[Page 864, Line 1 - Page 865, Line 10]

By Mr. Goodman:

Q What studies, Mr. Falk, have you made regarding the reasonable earnings the company should be allowed on equity?

A [Mr. Falk] It is a matter of the judgment of what earnings are necessary to cover the cost of interest on their debt, permit the payment of dividends and retain the portion of the earnings in surplus.

Q Yes, sir, but I have asked you: What studies have been made?

A I have made no particular studies of other transit companies, if that is what you are asking me about.



Q Have you made any statistical analyses or studies of any kind that underly your judgment?

A I have reviewed earnings-price ratios and pay-out ratios of certain transit companies as contained in the Public Utilities Fortnightly as a basis for arriving at my judgment, and the reason I say you can't rely on those -- you have a situation there of the stock of the Pittsburgh Railways, for instance, selling on the yield basis of 2.3 per cent. Actually, they lost money.

Q Were there a market for that stock?

A Well, it's traded on the market.

Q What standards have you, then, for allowable earnings on equity?

A I don't think you can apply standards of earnings-price ratios and dividend-price ratios in the case of transit companies. It is a judgment of what, in my opinion, is a reasonable dividend considering the small amount of equity that is in this company and the related risk of the debt capital over and above the equity capital.

Q And no statistical or analytical studies premise this conclusion of yours?

A That is correct.

[Page 868, Lines 2-20]

Q [By Mr. Goodman] What rate of return did you recommend for the transit company in the 1958 rate case?

A [By Mr. Falk] In the 1958 rate case I believe the fare structure adopted by the Commission resulted in a rate return of 6.17 per cent.

Q No, sir. I am asking you: What rate of return did you recommend?

A I would have to check on that. I recommended a fare structure that would result in a rate of return of 5.37 per cent.

Q And have the risks of D. C. Transit operations increased between that proceeding and this proceeding, in your opinion?

A I don't know that there has been any change in the risk.

Q Have you -- A There is more --

Q Excuse me.

A No; I don't know there has been any change.

[Page 953, Line 3 - Page 955, Line 20]

By Mr. Spiegel:

Q In connection with considering what a fair rate of return for the company should be, in your opinion should they consider the financial policies engaged in and practices of the owners of the company?

[ Mr. Roberts]

A / The Supreme Court says so.

Q And if that record indicates that through a series of holding companies and through the splitting of stock into two classes, that there is engaged in a transaction in which the grandparent company, Transportation Corporation of America, is making exceedingly high capital

gains by the sale of the stock, do you think that is something that should be considered in connection with fair rate of return?

A Normally, what is true is that with a utility the fact that the owners of the stock have bought it and are making a very high rate of return has nothing at all to do with the reasonableness of the return. That is normally.

Where you have a charter or unusual conditions, including certain present and future tax exemptions, as you have here, this is not the case. The fact that these unusual legislative advantages were given to this company as a part of its charter and that the purchase price of the property to the present owners was well known does have an effect in determining what the rate of return should be. In other words, if you know that the man acquired the entire property for one dollar and that subsequently, by efficient operation and by concessions in taxes and privileges of monopoly, he is able to attain a very large amount of money for his return, certainly you should not fix the rate of return on the same basis as if the actual property were developed by original investment of the owners.

I think there is a distinction between the normal determination of rate of return of a purely private company and the rate of return of a company which is actually a subsidy company such as this one here.

Q In other words, you would take into consideration the methods and facts as to the sale of the securities and the capital gains made by the grandparent company?

A I think you have to do that. You have to take the experience of the company, itself, and the cost of getting money for its operation. For example, if there are deposits maintained, as I understand is the case here, in large sums in certain banks for mixed purposes of securing credit, you definitely would take that into account in considering what was the interest rate for a funded debt or upon equipment.

Q The equity investment actually by the owners of this company in 1956, as I believe the record shows, was \$500,000. The dividends in each year since 1956, as I understand it, have equalled or exceeded \$500,000 a year. Do you know of any case in your experience of a public utility in which that kind of return has been made under regulation?

A I don't know of any case where it has been made upon substantially all the stock of the company. Individuals might have acquired stock at a very low price and had a very high return on it, but I have never heard of it being applied to an entire utility.

Q Is this something that should be considered?

A I have already said that. It definitely is an unusual condition which Congress knew and which the District Commissioners knew and with which this Commission is

confronted. It is a fact that renders unusual and extraordinary the attitude that should be taken both as to cushions and future protect -- protection from what -- and also with respect to the rate of return.

[Page 959, Line 21 - Page 961, Line 8]

THE WITNESS: [Dr. Limmer] I reside at 812 Malcolm Drive, Silver Spring, Maryland. I am a transportation economist in the Rates Division, Bureau of Air Operations, of the Civil Aeronautics Board. I am also a professional lecturer at the American University, having taught courses in transportation there on a part-time basis since 1949. I have also appeared as lecturer at the Institute of Industrial Transportation and Traffic Management and at the Rail Transportation Institute conducted by the American University, chiefly for executives. I have addressed the Institutes approximately since 1949. Between 1951 and 1954 I also taught transportation and business statistics at Southeastern University. I am a member of the American Economic Association and am listed in Who's Who in the east.

As for my education and earlier experience, I received my A.B. degree from Brown University, magna cum laude, in 1933; an A. M. degree from Columbia University in 1934, and a PhD. degree from American University in 1942. For all of these degrees I majored in economics, with a strong supporting minor in statistics. I wrote my doctoral dissertation in transportation economics. I was transportation

economist and statistician at the Interstate Commerce Commission from 1935 to 1938 and with the Department of Agriculture from 1938 to 1941, 1948 to 1951 and 1953 to 1956, and in 1941 a transportation economist with the Board of Investigation and Research. From 1946 to 1948 I was a statistician with the War Assets Administration and from 1951 to 1953 a statistician at the Office of Salary Stabilization.

From '42 to '46 I served in the U. S. Army, chiefly in the transportation corps as first lieutenant, discharged as captain. As an employee of the federal government, I have testified in several proceedings concerning cost of capital, rate of return and operating-ratio matters.

[Page 962, Line 15 - Page 966, Line 9]

THE WITNESS: [Dr. Limmer] My testimony will concern the fair return on equity D. C. Transit should be allowed the opportunity to earn and whether conditions would warrant use of operating revenues as a basis for fixing fares.

By Mr. Goodman:

Q What is the framework of your approach to the amount of net earnings a regulated enterprise should be allowed the opportunity to earn?

A Net earnings or profits are the rewards for risk-taking. In corporate enterprises net earnings are the compensation of those who invest equity capital. One task of a regulatory commission is to determine how much compensation



the investor should be allowed. Under the cost-of-capital method that I espouse a reasonable return to investors is simply another cost of doing utility business. The objective of permitting regulated enterprises to realize adequate amounts of earnings is, in addition to providing justice to the owners and other capital, to assure that needed capital will continue to flow to such enterprises. The task of the regulator is to find that rate of return on investment which will make the utility an attractive investment to private investors. The question, then, is: What is the proper measure of the earnings that the investors require the utility to earn as a prerequisite to investing?

The question is not what the utility should theoretically be permitted to earn because of the theoretical risks involved in the corporate operation, but, rather, the question is: What return do investors demand or what return must be earned to attract capital on favorable terms.

Q Dr. Limmer, before we enter into the details of your computation, would you summarize for us your technique for measuring the earnings that must be earned before prospective investors will supply additional equity capital to an enterprise and specifically to D. C. Transit?

A Although I will speak generally, each of my statements will apply also to D. C. Transit. The earnings required by equity investors may be obtained by determining what investors

pay in the market for the company's earnings. By comparing the company's stock market prices with the profits that are being earned we obtain the most objective standard available to measure the cost of equity capital. Under the cost or supply price of capital approach for common equity capital, the valuation placed upon the transit company's earnings by the investor is, in fact, determined. The conventional method of testing the earnings requirements of the equity investor is the earnings-price ratio, which is defined as the ratio of available earnings to the market price of common stock. For example, if a business has earnings of five dollars per share and each share sells for \$50, its earnings-price ratio is 10 per cent. The earnings-price ratio embodies the investor's own appraisal of all the factors which motivate his decisions. It takes all factors into consideration insofar as the investor can weigh them. It indicates the price which the borrowers--"borrowers" in quotation marks--of equity capital must pay to get equity capital, and this price is also the supply price which is demanded of the transit company. In this market price the investor reflects all his hopes and fears. Whether or not the market correctly evaluates these factors is not controlling. What is of real concern is the measurement of the terms and conditions under which investors will offer their capital to the transit company. All that is required is to measure the supply price of equity capital for the near future with a reasonable margin of safety.

Here in the market place of capital investors in both debt and equity will weigh the relative risks of the enterprise and demand their supply price based on their evaluation of these risks. Thus, the computed cost of capital will reflect all the elements of risk affecting an enterprise that are relevant to the fair return on investment the utility should be allowed the opportunity to earn.

Q How does the company's past and projected program for converting the streetcar operation to a bus operation affect the cost of capital or the recommended return on equity capital?

A I make no separate allowance in the return on equity for any specific part of the conversion program or for any conversion schedule. To the extent the conversion program requires the company to obtain additional capital, be it debt or equity, the rate of return based on the cost of debt and equity capital will permit attracting additional capital on favorable terms. If a company is permitted the opportunity to earn more than its cost of capital, it is permitted to earn a windfall and the transit rider is overcharged. The only standard that is fair and reasonable, from both the company and transit rider standpoints is the cost of attracting capital, that is, the rate of return that must be allowed for the company to attract new capital on favorable terms.

[Page 968, Line 5 - Page 969, Line 4; Page 970, Lines 3-16]

[By Dr. Limmer] Market data which might directly measure D. C. Transit's cost of equity is available only from May 1959 to the present. These data indicate that D. C. Transit's current ratio is around 3 per cent, but the period is not long enough to permit me to say that the company should earn 3 per cent on its equity. It does indicate a very favorable current market. I have analyzed — instead of taking D. C. Transit's ratio, I have analyzed 11 local transit companies to obtain a cost of equity to apply to D. C. Transit. These companies were chosen to represent the operations of relatively large companies comparable in general with D. C. Transit.

I have selected companies with average gross revenues of approximately \$10 million or more during the 1952-58 period, with earnings in all or practically all of this period and representing predominantly local transit operations. I included the data for Capital Transit for the period '52 to '54, although usable data were available only for three of the seven-year period because such inclusion permitted a comparison with the parent company of D. C. Transit. The companies covered in the analysis were, in fact, every transit company operating in the United States with the foregoing characteristics for which data were reported in Moody's Transportation Manual for 1959.

\* \* \*

I have decided, for this purpose, to use the unweighted arithmetic mean as the most appropriate average of earnings-price ratios here analyzed. It is, as you know, the highest of the averages which may properly be used. It should be noted that the Baltimore Transit Company, operating a relatively near-by community of about the same size as Washington, had an average earnings-price ratio of 9.53 per cent. Capital Transit had an average of 6.70 per cent during the 1952-54 period -- I did not count '55, a negative price ratio, because of the lengthy strike that year -- and the figure for Capital Transit during the 1948-54 period is 8.47 per cent, during this period, during which there were earnings in every year.

[Page 972, Line 6 - Page 973, Line 24]

Q [By Mr. Goodman] Dr. Limmer, what fixed charges protection will your recommended equity rate provide?

A [Dr. Limmer] As shown on Page 4 of Exhibit 43, my recommended return on equity capital for D. C. Transit will provide coverage of present fixed charges by four times. As a frame of reference, it should be noted that New York State Insurance Laws, Section 81, requires for unsecured debt to be legal for insurance company investments that income before income taxes be equal at least to 1.50 times interest on the average during the past five years. At the equity rate I recommend D. C. Transit's income before

income taxes will cover present fixed charges by four times. However, this substantially understates the times protection afforded the debt holders in emergencies.

Debt interest does not have to be paid from earnings but from cash available. It has long been recognized that depreciation is a source of cash which is available for any corporate purposes and constitutes a strong safety factor in an emergency. Moreover, the real protection afforded fixed charges is understated by the 4.0 figure in that contractability of transit of nonfixed expenses is not therein reflected. To the extent that the company is able to contract expenses, there is additional revenue made available to cover fixed charges.

Q What other factors have you considered, Dr. Limmer, which reconfirm the reasonableness of your recommended return on equity of 12.55 per cent for D. C. Transit?

A There are several. First, the fact, as shown on Page 2 --

Q Three.

A -- of Exhibit -- Oh, Page 3. --Page 3 of Exhibit No. 43, that the company's current earnings-price ratio is running around 3 per cent, using the parent's ratio to indicate what the local company could command in the market, shows that an 11.13 per cent earnings-price ratio is more than ample for the immediate future. Secondly, the recommended figure is much higher than for the average transit



company, the average return, that is, a return on equity for the average transit company. The average return on equity of 26 leading traction and bus companies for 1958 was 4.4 per cent, as reported in the First National City Bank's of New York Monthly Letter for April, 1959.

[Page 978, Line 1 - Page 979, Line 1; Page 979, Line 13 - Page 983, Line 20]

Q Dr. Limmer, would investors compare operating ratios as among various industries?

A [Dr. Limmer] No. The operating ratio provides absolutely no basis for a valid comparison between or among industries. A high operating ratio may be characteristic of one industry and a low operating ratio characteristic of another. Furthermore, the operating ratio provides no clue to the profitability or relative risk of the enterprise. The ultimate investor test is the rate of return earned on investment.

Take, for example, various retail stores. It is well known that grocery stores have a very high capital turnover. I believe approximately 12 per cent. They turn their stock very rapidly. Their stock does not stay on the shelves very long, and this is especially true for chain grocery stores. On the other hand, jewelry stores turn their capital over much more slowly. Obviously, you can't sell jewelry as fast as you can groceries. Now, therefore, it is absolutely essential for a jewelry store, in order to make the same

profit on an investment as a grocery store, to have a much higher margin per unit of sale. Their margins, I believe, are about 50 per cent or even more. On the other hand, the rate of per cent of margin on sales of chain stores, food, in 1958 was 1.4 per cent, as shown in Exhibit 46, Page 1, which is obtained from National City Bank letter.

\* \* \*

By Mr. Goodman:

Q Would you explain, Dr. Limmer, how this exhibit [46] shows the lack of correlation between operating ratio and profitability?

A Well, you can easily see that it is possible to have various industries with approximately the same margin of sales which have widely ranging rates of return on investment. For example, I direct your attention to the industry entitled "Hardware and Tools", which is approximately one-half way down the page, Page 1. Now, you will notice that the hardware and tools industry has a per cent margin on sales of 4.0 and a per cent return on net assets of 6.2. Now, for other metal products, which has the same per cent margin on sales of four per cent, the per cent return on assets is 9.1. Miscellaneous transportation, which has again the same per cent margin on sales of 4.0 -- the per cent return on assets is 9.6. With only an increase in per cent margin on sales of one-tenth of one per cent, which is the situation for tires and rubber products, the per cent return on assets is 10.5

per cent. For electrical equipment, radio and television, skipping one line, the per cent margin on sales is 4.2 per cent; the per cent return on net assets is 12.2. Then for machinery, which is the last line that I am going to direct your attention to, which is a few lines down, the per cent margin on sales is 4.3 per cent and the per cent return on net assets is again 8.0. So, in the interval of between 4.0 per cent and 4.3 per cent as per cent margin on sales the per cent return on net assets ranges from 6.2 per cent for hardware and tools to 12.2 per cent for electrical equipment, radio and television.

Q Is it your conclusion, Dr. Limmer, that the operating ratio provided no valid measure of the earnings a regulated enterprise should be allowed the opportunity to earn?

A Yes. There is no available standard for determining the reasonableness of utility earnings except the cost of money. The cost of money is the only proper measure of the earnings a regulated enterprise should be allowed the opportunity to earn.

Q The question is sometimes heard, is it not, that in enterprises such as public transit, in which the capital investment is small in comparison with the volume of operations, the risk is more properly measured by the annual volume of the revenues rather than the investment?

A The answer to this argument is that no matter how often the capital is risked because of its high turnover--

"risky" in quotation marks--the amount of risk is limited by the amount of capital. It is odd, indeed, to assert that the less the capital the greater the risk because the capital turnover is higher. According to this reasoning, the risk presumably would be highest for the utility with no capital investment, all of its equipment being operated under lease.

In the words of Allan H. Willett in "The Economic Theory of Risk and Insurance", Page 42:

"In just what sense a man can be said to run a risk of loss who has nothing to start with and who, therefore, cannot fail to come out from his venture at least as well off as he went in, it is not easy to understand. Only those who have capital can suffer the loss of capital."

An extreme example will illustrate the point I am making: The example is that of a man renting a small space in a retail store to sell fruits and vegetables. Let us assume that his total capital investment consists of a scale which cost him \$25, plus \$100 which he uses to buy fruits and vegetables. Let us further assume that he buys a hundred dollars' worth of produce every morning, which he sells before the end of the day without spoilage. If the man works 300 days a year, his total annual expenses are \$30,000. What would be a "fair" level of net earnings for him in addition to a fair imputed wage, including the so-called wages of management? Shall the return on his investment be a certain percentage of \$30,000 or of \$125

or, let us say, if he had an imputed wage of \$4,000, a certain percentage of the \$34,000?

Obviously, at any time he cannot lose any more than his capital investment of \$125. If he borrows \$125 to buy his scale and produce, he pays a certain amount of interest, whether high or low, based on the money borrowed, regardless of how often he spends it.

If it is decided to allow him even one percent of his operating expenses, excluding imputed wages, his net profit would be \$300 for a capital investment of \$125.

A ten per cent return on his operating expenses would be \$3,000. A ten per cent on his actual investment would be \$12.50. These net earnings are, of course, to be added to a fair imputed wage. Similarly, a fair level of net earnings for the D. C. Transit System cannot properly be computed on the amount of the operating revenues which for the 12 months ended September 30, 1959 amounted to 27.7 million dollars. Obviously, at any time the company cannot lose any more than its capital investment of 6.3 million dollars. It is these 6.3 million dollars which bear the risks of the enterprise and which must be afforded the opportunity of earning a fair rate of return. Of course, this return will be in addition to coverage by revenues of all properly incurred operating expenses and taxes, which in this case

will include a salary paid to the prime investor of \$40,000 per year.

[Page 990, Line 14 - Page 997, Line 19]

COMMISSIONER KERTZ: I didn't follow you in that last statement.

THE WITNESS:[Dr. Limmer] My point is this, Mr. Commissioner: That when a utility, another company, rents equipment the rental that it pays always includes a profit element to the lessor. Now, if the utility is allowed a return on the revenues gained from the leased equipment, the public pays the capital cost twice, once to cover the return element of leasing expenses and again as a percentage of the return element because the operating ratio, you see--

COMMISSIONER KERTZ: Is that, in your judgment, something that we should correct?

THE WITNESS: I think that is paying excessive capital costs. In other words, if the company owned -- Go ahead, sir.

COMMISSIONER KERTZ: Doesn't that apply to practically everything that we deal with each day? Isn't there always a middle man or a producer, --

THE WITNESS: The return on investment --

COMMISSIONER KERTZ: --wholesaler or--

THE WITNESS: No. I'm afraid I didn't make myself clear, Mr. Commissioner.



COMMISSIONER KERTZ: No. I am not clear. That is why I am asking.

THE WITNESS: Yes. You see, the return-on-investment method requires that the return be computed on the invested capital.

COMMISSIONER KERTZ: I understand that.

THE WITNESS: Now, when the operating-ratio method, in fact, requires that a return be a percentage of the amount of operating expenses or, which is the same thing, a percentage of the operating expenses -- I said operating expenses -- I meant operating revenues, which is another percentage of the operating expenses. In other words, the operating-ratio method can be either a percentage of the operating expenses or a percentage of the operating revenues. In other words, an operating ratio of 90 per cent, for example, gives a profit margin of 10 per cent of revenues. That can be expressed as an operating margin of 10 over 90 or eleven and one-ninth per cent of expenses.

COMMISSIONER KERTZ: Yes.

THE WITNESS: Now, if the expenses, Mr. Commissioner, include a return element in them the public pays twice. They pay in the expenses, and then they pay 10 per cent of the expenses as additional capital costs.

COMMISSIONER KERTZ: I am sorry. I don't follow you on that, but go ahead.

By Mr. Goodman:

Q Dr. Limmer, following up the Commissioner's question, isn't it true that this 10 per cent of the expenses, the expenses which include a cost of capital of the lessor, is added on to the return that the company is allowed to earn, which return has been computed after deducting all allowable expenses?

A That is right. May I -- I wonder if I could give just another example to make things a little clearer. Let us assume you have a company which leases all of its equipment and all of its expenses consist of that rental. Let us say it rents that equipment from Company A. A, let's say, charges this company \$90,000. In that \$90,000 there is an element of profit for Company A. Now, Company B turns around and it makes a charge to Company C. Now, it will charge under the operating-ratio method, let's say, 10 per cent of \$90,000. Now, let us assume in the original \$90,000 there was a ten-thousand-dollar profit to Company A. That means that Company C., then, or the public, pays 10 per cent of \$90,000 which includes also a 10 per cent of 10 percent of the profit element which is in there. So, instead of paying 10-90 of profit or eleven and one-ninth per cent profit, you have that profit plus 10 per cent of 10 per cent or one more per cent. You have 12 per cent instead of 11 per cent. I don't know if that makes things any clearer to you.

Q Dr. Limmer, why is the rate of return on investment the proper method of measuring the adequacy of the return element?

A The rate-of-return-on-investment method falls within a frame of reference. After covering the utility's operating expenses, this method gives the utility a number of dollars that can be judged against the cost of raising the utility's capital, that is, the number of dollars that is required to rent or borrow money, the number that is needed to enable the utility to keep its promises to the preferred stockholders, if any, the number required to keep the common stock in good standing in the market and to enable the utility to attract more capital when and if it later appears that such capital is needed and can be advantageously used. Whether a rate of return is reasonable or not can be definitely ascertained.

Moreover, this rate of return on investment does measure the return to investors. Investors are chiefly concerned with the percentage that their return bears to their investment. In fact, they are wholly concerned with that, consistent with safety and with possibilities of increase in their capital, the capital value of their investment. This is the decisive point to them. Whether the business has the high operating ratio and rapid capital turnover of a chain grocery or the low operating ratio and slow capital turnover of an electric utility is only of

secondary interest to them. Investors are chiefly interested in the number of dollars they get in dividends and in appreciation in the value of their investment in relation to what they put in, giving consideration to security, stability, and so forth. Investors can and do make comparisons of returns on investment among various industries and companies. They can and do contrast the yields being recorded in the securities' markets as the result of a free and independent action of willing lenders and willing seekers of capital. The method of obtaining the proper rate of return on equity capital by use of the earnings-price ratio results in giving full allowance for all of the characteristics of the enterprise. The earnings-price ratio also considers the future outlook and the risk of the enterprise, its hopes and its fears.

The impartial securities' market takes these factors into full account in its capitalization ratios. It establishes equilibrium between optimism and pessimism with respect to risk of the industry. If the transit company is to be compensated for its costs, these costs should properly include the cost of capital. The profit margin and the operating ratio give no help in determining these capital costs, which can be determined only with respect to the amount of capital invested.

Q Do conditions now warrant a shift to the operating revenues as a base for the determination of a fair return for D. C. Transit?

A There are no conditions which now warrant such a shift.

Q What are your over-all conclusions, Dr. Limmer?

A I conclude that a fair and reasonable return on equity for D. C. Transit is 12.55 per cent and that there are no conditions which warrant a shift to operating revenues as a base for setting rates or use of an operating-ratio standard. Thus, based on equity capital as of September 30, 1959, D. C. Transit should be granted the opportunity to earn a return of \$335,322 for equity. Assuming the staff's estimate of \$316,657 of interest expense during 1960 is reasonable and accurate, the company should be allowed the opportunity to earn net operating income or a total return of \$651,979 for debt and equity combined.

Q Dr. Limmer, finally, are there any cushions over and above this return allowance that the Commission should grant D. C. Transit an opportunity to earn?

A Yes; there are significant cushions. One is --

Q Excuse me. You misunderstood my question.

A Excuse me.

Q Are there any cushions which the Commission should grant over and above this allowance?

A No; there are not.

Q And why?

A Because -- and I misunderstood your question before -- I have liberal cushions or margins imbedded in the ratio

that I recommend. For one thing, this ratio of 12.55, which I applied to the entire equity includes, as I have already indicated, applying the cost of acquisition to the surplus accounts in addition to the equity capital. Secondly, I have chosen a very liberal average to give to D. C. Transit. Thirdly, a comparison of the figure I have recommended with the actual earnings of Capital Transit, either the entire '48 to '54 or the '52 to '54 period, shows that the percentage I have recommended is liberal.

Q You state, Dr. Limmer, you have applied the cost of acquisition to the surplus account and that this is a cushion. Why is that so?

A Because that has not been obtained from the market place. In other words, the proper restriction of acquisition cost is to apply it only to the capital that has been obtained in the market place, which is the capital stock account, itself.

[Page 1000, Line 2 - Page 1005, Line 16]

By Mr. Spear:

Q On Exhibit 46 your second item is 26 traction and bus companies. Do you have a list of those, sir?

A [Dr. Limmer] No, sir; I don't.

Q Were these mostly traction companies or mostly bus companies, or do you know?

A I don't know. I have made an effort to obtain this list from the National City Bank and was unable to do so.



Q Do you have the list of all of the companies on Exhibit 46, sir? Do you have work papers to support Exhibit 46?

A What I have is the copy of the National City Bank letter that produced that, in which these figures are shown as such.

Q May I see it, sir? Have you checked any of the figures on Exhibit 46? Have you checked them against the original sources of information?

A I have not.

Q Do you know the basis for selection of these corporations, other than the title at the top of the list?

A All I know is what the title says, which is that they are leading corporations.

Q One other question, Dr. Ezekiel Limmer: You talk of cost of equity capital. Do I understand your phrase to mean the percentage on what you call equity that the return bears to that equity? Is that what you call cost of capital -- the per cent return upon equity?

A If I understand you correctly, yes.

Q Is that not the reciprocal of the so-called price-earnings ratio? I am sorry. Let me withdraw that question. When you talk of equity, do you talk of equity as evidenced by the market price of publicly held stock?

A The term "equity" to which the earnings-price ratio is applied is the account in the corporation's books which

includes the surplus and the capital stock accounts.

Q How about Page 2 of Exhibit 43? Aren't those ratios all related to market price of stock as distinguished from the equity you have just defined?

A Yes. In other words, I find out what the relationship is between earnings and prices and apply this earnings-price ratio to the equity on the company's books. You see, in other words, the earnings-price ratio indicates how investors evaluate earnings of the company. If the price -- Let me put it this way: If a stock sells at precisely its book value, then the earnings-price ratio would be exactly the earnings on equity. The only difference between earnings-price ratio and the return on equity is the difference between the price and the book value per share.

Q What would you say the equity, from your definition, of D. C. Transit System, Inc. is, shall we say, as of December 31st, 1959?

A December 31st?

Q The end of 1959. What is the figure which would be equity, as you define it, for purpose of your Exhibit 43?

A The only figure I have for the equity of D. C. Transit is the figure as of September 30, 1959.

Q Which figure are you using there? A On Page 4.

Q Is that the one on the bottom of Page 4?

A Page 4 of 43. That shows a total of \$2,671,889.

Q What adjustment do you make to reflect the fact that on the market-price basis some 15 per cent of the stock of the parent, which is the only publicly held stock, is selling at a price of three and a half million dollars and that is only 15 per cent of the equity stock of the D. C. Transit of Delaware? What adjustment do you make for the fact that on 15 per cent of three and half million dollars the market is valuing D. C. Transit at about seven times three and a half million dollars or at about 24-1/2 million dollars?

A I am glad you asked me that question because in the utility regulation you should never fix returns on the price of the stocks because the price of the stocks depend upon the earnings. What we are trying to do here is to determine what the reasonable earnings should be. Now, the price depends upon the earnings. You can't go around and fix the earnings based upon the price. Therefore, we have to neglect the market price of the stock as a base and to to the invested capital, not what the invested capital is selling for in the market place.

Q I am not suggesting that is a factor here, but I am suggesting that you are using a market-price ratio on Page 1 of Exhibit 43, and I don't see how you jump from Item 1 or Line 1, as you call it, to Line 4. I am trying to see how you jump from market price of the parent company's stock to equity, as reflected, shall we say, by

that stock. I, frankly, don't see the connection between the two myself, but I am trying to see how you tie the two together with your 112.76 per cent.

A Okay. You mean that cost of acquisition cost or --

Q I am trying to see how you tie them together. Is that the way you tie them together? A No. Q By that factor? A No. Q Or is it another factor? A No.

Q Or are they tied together?

A They are tied together in this way: The earnings-price ratio shows the rate of capitalization that investors place upon utility earnings. If, for example, as I indicated, a company has a price of \$50 and earns five dollars, that means that investors have a relationship or are placing a relationship of price of 10 times earnings or an earnings-price ratio of 10 per cent. Now, the question is-- the point is this: If the price happens to be equal to book value, then there's a very easy transposition, as I have indicated to you, between taking that earnings-price ratio and applying it to the equity and, consequently, coming up with the proper return on the equity.

If the price is different -- let us say for the moment the price is considerably higher than the book value. That indicates somehow the earnings of the company, you see, are valued at a much lower capitalization than earnings indicate. For example, if, let us say, that book value is a hundred dollars; the company is earning, let's say,

10 per cent on that book value; if the price happens to be \$200, that means that the market -- the 10 per cent, let's say, is \$10 a share, 10 to a hundred -- that means the market is evaluating those earnings at five per cent -- 10 divided by 200. So, it is evaluating the earnings, you see, much less than the company is actually earning on its equity and, consequently, five per cent is the proper evaluation or is the proper rate of return the company should be allowed to earn on its book value of \$100.

[Page 1011, Lines 1-7]

Q [By Mr. Spear] Do you generally oppose the theory of operating ratio in rate proceedings? Is that your personal view?

A [Dr. Limmer] Yes.

Q Have you ever read the Public Utility Law of the District of Columbia?

A No.

[Page 1013, Line 25 - Page 1014, Line 2]

Q [Mr. Spear] Have you ever read the act of July 24, 1956 by which D. C. Transit was given a franchise?

A [Dr. Limmer] No; I have not.

[Page 1031, Line 1 - Page 1033, Line 20]

By Mr. Bebachick:

Q Mr. Harris, will you kindly explain Page 1 of Exhibit 51?

A [Mr. Harris] The purpose of this exhibit is to show

the adequacy of the present reserve provision balances on the books of the D. C. Transit System, Inc. at September 30, 1959, to provide fully against the expenses to be incurred for track removal, repaving and the final disposition of all rail properties, including all remaining depreciable value of those properties on the books of D. C. Transit as of September 30, 1959.

The reserve provisions on the books of D. C. Transit at that date were the reserve for track removal and repaving in the amount of \$3,216,286. The unamortized balance of original equipment acquisition adjustment — going over that again, the unamortized balance of the original acquisition equipment adjustment of \$10,339,041 was \$7,108,091 at the September 30, 1959 date, providing a total reserve on the books of the company of \$10,324,377. Deducting the undepreciated cost of the rail properties of D. C. Transit at September 30 in the amount of \$5,121,644 left a remaining provision or reserve of \$5,202,733 to provide for track removal and repaving expenses.

Q Sir, in this computation you include the unamortized balance of the original acquisition adjustment as a reserve to provide for the disposition of these properties and the remaining work to be done in track removal and repaving. Why do you so treat the acquisition adjustment in this fashion? I see Mr. Spear desires enlightenment.



A Although it is denominated an acquisition adjustment account, it serves the same purposes as any other reserve account, as any other reserve provision. It is a provision against, in this instance, the remaining book value of the real properties. It is, in effect, the same as accrued depreciation and has to be so treated, I believe, by the Commission's staff. It is a hole in the assets. It is a diminution of the original cost of the assets, the same as accrued depreciation.

Q What did the acquisition adjustment originally constitute? What was it, this figure of \$10,339,041? What does it represent?

A That original adjustment, of course, goes back to the difference between the purchase price paid by D. C. Transit for the properties of Capital Transit and the net asset values on the books of Capital Transit at August 14, 1956. Before going into that, I would like to explain further as to this \$5,202,733 and what that net reserve provision amounts to when related to the liability for track removal and repaving.

The exhibit shows that this remainder is equivalent to a gross provision for track removal and repaving of \$11,388,224, less the income tax credits of 54.3148 per cent, amounting to \$6,185,491 -- returns us to the net remaining provision applicable to the removal of tracks and repaving. That is, this exhibit shows that the value of

all the rail properties, that remaining value of \$5,121,000 and the necessary provision for the liability of track removal and repaving, has already been taken care of on the books of D. C. Transit, that the fare payers have already borne the burden of this loss in rail values and this cost of track removal and the repaving, and that no further recognition should be taken of rail property values in the property rate base and that no further allowance should be made for rail property depreciation for the purpose of fixing rates for D. C. Transit.

[Page 1035, Line 5 - Page 1038, Line 21]

[Mr. Harris] My approach to the original valuation of the original purchase differs somewhat from the opinion of Mr. Flanagan, which I will explain. Under the terms of the new franchise, providing for the removal of tracks and repaving and the implicit condition of the discontinuance of rail operations, the new purchaser, of course, adjusted his purchase price bid in the light of this condition. First, he had to evaluate the cost of removing the tracks and repaving, the extent of his liability, and he had to adjust his purchase bid downward to the extent of his net liability that he was assuming to remove the tracks and repave.

Secondly, he is bound to have looked at the remaining book values or the remaining rail property values on the books of Capital Transit and concluded that they were

valueless and that the purchase price would be further reduced to the extent of any value at that time on the books of Capital Transit for rail properties.

Now, let's go back. The purchase price was \$10,339,000 less than the net asset value shown on the books of Capital Transit. If the purchaser in arriving at his purchase price estimated a liability, a gross liability, for the removal of tracks and repaving in the amount of \$10,000,000 and knowing full well that for every dollar of expenditure he would get a tax credit of 54 cents plus, or 54 per cent, he would, of course, evaluate his net liability that he was assuming at approximately \$4,600,000. That would leave, out of the \$10,000,000, some \$5,400,000 to apply against the book values of the rail properties.

It is my contention that that explains the difference between the bid price and the net book asset value shown by Capital Transit and it indicates that the purchaser paid the net asset value of Capital Transit after the \$10,000,000 downward adjustment with respect to rail properties.

Q Mr. Harris, I notice in this exhibit that you take the value of the various reserves and you make your computations on the basis of September 30, 1959. Why have you selected this as the period upon which to base your recommendations for the future rather than going back to 1956?

A I took the balance sheet which, I believe, is Exhibit 16 in this proceeding because it was the latest balance sheet that I had available. As to the reason I did not go back to August 15, 1956, the reason is that that is all water over the dam, and there can be no retroactive application. You have to take the company as it stands today and go from there.

Q Is it not true, sir, that in a sense the amortization of the acquisition adjustment and the charge to the reserve for track removal balance themselves out so you have a net figure left which is almost within a few dollars of being identical with the original amount of the acquisition adjustment back in 1956?

A Yes, sir; I think that is very significant. I think that indicates that in fact this entire accounting operation is just that, an accounting operation. That is, amortizing the acquisition adjustment and setting up close to the same amount each period as an accrual -- as a reserve provision for the track removal.

Q I would like, if you would, Mr. Harris, to have you explain to the Commission how you calculated the gross provision for track removal and repaving on Page 1 of Exhibit 51. It is the third line in the body of the exhibit. Just tell the Commission how you computed that.

A That arises from the fact that we have a net remainder of these two reserve provisions on the books at

\$5,202,733 at September 30, 1959. In order to determine what gross provision for track removal and repaving that amounts to, it is necessary only to deduct the effective tax rate from 100, getting a percentage of 45.7, approximately, dividing that 45.7 into the \$5,202,773, which gives your gross provision, and then working back around the circle you deduct the income tax credit of 54.3148 per cent and, of course, you arrive back at your net remainder available for track removal and repaving.

I might add that 54.3148 per cent income tax represents the deduction of a 4.60 per cent D. C. Transit and a Maryland tax of .2225 per cent. Deducting those two taxes from the total expense and then computing 52 per cent on the remainder.

Q It is a constructed figure, then?

A It is a constructed, composite tax figure.

Q And I take it the income tax is the income tax that would be allowed when the actual expenses were incurred in track removal and repaving as they are incurred by the company?

A Ordinarily, that is the case. The accrual of any such provision is ordinarily not allowed by the Internal Revenue Bureau. As I understand, they have not been allowed by the District of Columbia tax people.

[Page 1039, Line 24 - Page 1040, Line 24]

Q [Mr. Bebachick] Mr. Harris, have you had an opportunity to examine a statement of the expenses incurred in 1958 and 1959 by the company for track removal and repaving?

A [Mr. Harris] Yes, sir. I have a photostatic copy of the charges to the reserve account.

Q Which was provided by the company counsel?

A Yes, sir.

Q Mr. Harris, will you kindly inform the Commission what the expenses were experienced by the company for; track removal and repaving in the years '58 and '59?

A Yes, sir. This photostat shows total net charges of \$12,735,000 in 1958.

Q Not \$12,000,000. It is \$12,000,000?

A I beg your pardon -- \$12,735 in 1958. It is \$48,602 in 1959, or a total of \$61,338.

Q Mr. Harris, could you repeat that figure for the reporter, please? I believe you stated it in millions.

A It is \$61,338.

Q Could you provide us with a breakdown?

A Turning to the total expenses incurred, we find that the company entered \$24,288 to the reserve provision in 1958, and \$135,909 in 1959, the difference being explained by the realization of \$98,869 in salvage over the two-year period.



[Page 1055, Line 15 - Page 1056, Line 11]

Q [Mr. Bebachick] Sir, does the group method of depreciation compel you to continue to fully depreciate fully depreciated buses, or are there accounting techniques available to eliminate such fully depreciated buses from the method of accounting?

A [Mr. Harris] Yes, sir. There is a method of eliminating the original cost of fully depreciated properties by charging the retirements of individual items back on a first-in-first-out basis. That is, upon the retirement of a bus, its original cost would be tabulated opposite the first original cost entered on the property account. In that way, you would keep an accounting of acquisitions during each month over the period of years, or during each year over the period of years, and those net amounts in the original property cost would be dropped from the depreciation base as the 14-year service life period elapses.

Q This is known as moving the line down?

A Yes, sir.

COMMISSIONER KERTZ: Have you used that type method?

THE WITNESS: I used it at Braniff Airways, of course.

[Page 1076, Line 22 - Page 1078, Line 20]

Q [Mr. Goodman] And I understand that you have a few corrections to make in your exhibits this morning?

A [Dr. Limmer] Yes. In my Exhibit Number 43, on Page 2, through an inadvertence I omitted two companies:

The Niagara Frontier Transit Corporation and the Fifth Avenue Coachlines, Incorporated. I would like to read the averages for those two companies and make the other corresponding changes in the other figures. The Niagara Frontier Transit Corporation which operates around Buffalo is first and the earnings-price ratio percentages are as follows: For 1952, 27.0; for 1953, 31.6; for 1954, 4.4; for 1955, 17.8; for 1956, 3.3; for 1957, 9.5; for 1958 it was a negative price ratio and so I called it zero; the average for the seven years is 13.37.

For the Fifth Avenue Coachlines the earnings-price ratio, also expressed in percentages as the other one was, is as follows: For 1952, 15.6; for 1953, 9.2; for 1954, 12.4; for 1955, 10.0; for 1956, 7.6; for 1957, 10.4; for 1958, negative earnings-price ratio so that, of course, is zero. The average for the entire seven-year period is 9.31. This changes the annual averages as follows and the corrected figures are these: For 1952, 14.86; for 1953, 15.07; for 1954, 10.80; for 1955, 10.67; for 1956, 7.40; for 1957, 11.23; for 1958, 8.07.

The average for the entire period is 11.16, which is three-hundredths of one per cent different -- a little higher than the previous one of 11.13. Going back to Page 1, indicating the cost of equity, this becomes 12.58 instead of 12.55. Let me point out in my testimony I indicated the median as 10.7 and based on the latest figures that is 10.13.

The time-weighted mean average was, as I indicated, 10.40 and, the figure based upon the 13 figures, is 10.43.

There are slight changes on Page 4 of Exhibit 43 and Line A, the line should read: "Line B-3 plus 12.58 times 42 or \$5.28."

The last figure should be \$9.05 instead of \$9.04, and these changes then make my final figure as to the return, the proper return for equity capital, which I had before as 335,124, should now be 336,124.

CHAIRMAN HAYES: On what page is that?

THE WITNESS: That was in my testimony, Mr. Chairman, and the total return, including interest of 316,657 should be 652,781 instead of 651,979.

[Page 1092, Line 15 - Page 1096, Line 20]

Q [Mr. Spear] And I ask you, sir: What relevance has a non-priority mail pay case to a case involving the transportation of people by a public utility?

A [Dr. Limmer] The principles are identical.

Q What principles?

A In other words, the principles of obtaining a proper return on capital are identical. I mean: Whether you have a public utility or a gas or electric company, a transit company carrying passengers or an airline carrying passengers, or non-priority mail, it doesn't make any difference what you carry.

Q Are the problems of transporting passengers over scheduled routes at scheduled times the same as problems of carrying non-priority mail on airlines?

MR. GOODMAN: Would counsel please define what he means by "problems"? I am afraid he is going beyond the direct testimony of my witness whose testimony is concerned with the cost of equity capital and the operating ratio.

MR. SPEAR: I certainly am going beyond the direct testimony, Mr. Chairman, because the direct testimony was about non-priority mail. I am trying to show it has no bearing on this case. I necessarily have to go beyond the testimony to show that it doesn't apply to our case, and I am trying to compare non-priority mail cost of capital studies with this case and find out what the relevance is. I believe the question is quite clear.

CHAIRMAN HAYES: We will allow the question, Mr. Goodman. We understand the word "problems" and the witness has not indicated that he doesn't understand or that he has any difficulty understanding the question. Do you understand, Witness?

THE WITNESS: Yes; I understand the problem with respect to capital; that is why we are trying to compare these two and the principles are exactly the same whether the company carries materials or passengers or mail or whether it is a gas-producing company, such as an electrical company, or anything else. That is what we are trying to do. It is immaterial as to the precise nature of the business when it comes to capital market.

Mr. Spear, all these companies are competitive. They go into the capital market and they have to pay a price for it and that is what I am testifying to in this particular case.

By Mr. Spear:

Q Are you suggesting that we compete for capital in the market place with a produce dealer and those people you have listed in this exhibit, the non-priority mail carrier and the local retailer and the cobbler and everyone else?

A No; I wouldn't say that. What I am saying is this: That there is competition among like businesses for capital. As a matter of fact, on the priority or non-priority mail carriers, this is exactly the same as the carriers that carry passengers, and what I am saying is this: That companies of similar types as Capital Transit would compete for capital with them, and companies of approximately the same credit rating, I'd say, or, as a matter of fact, competing companies in general -- they compete with companies in general -- although they would not compete, of course, with little businesses which depend upon the capital of their owners, but they would compete with other businesses, regardless of that fact.

Q But does not the risk, capital vary with the other risks involved in the particular business, such as the particular problems of the community, the stability of the earnings, the nature of the industry -- whether it is a

transit company, on the one hand, or a motor producer, on the other hand? Are those not all factors that affect the cost of capital?

A Well, they certainly are, Mr. Spear. That is what your earnings-price ratio is intended to do, by going to the market place and determining how these investors price themselves -- what actual prices they would have to pay and what they are willing to pay for the earnings, actually, in price. That is how an investor evaluates risk, as expressed in the free and open competitive market.

Q But are not the issues in the cost of capital for transit companies generally different from the issues that determine the cost of capital even in priority mail carriers, for example?

A No; the issues are identical. The prices may be different.

Q They would be different -- the prices would be different?

A Well, of course, every business is unique. Every business is unique. You can't compare one business with another in every single respect, but you can generalize. I think it is possible, for example, to compare the transit companies, in general, but that is what I do over here. If it were possible, frankly, I think it would be preferable to obtain figures on Capital Transit, as such, but we couldn't do that. The figure obtained was for such



a very short period that it would come to a very low figure of three per cent and obviously we couldn't use that.

Q But what is the applicability of all of the numerous kinds of industries that go all the way from beer brewers to transit companies on Exhibit Number 46?

A Well, the sole purpose of this was to show that there is no relationship between the operating capital and the return on the assets. I didn't use it to any extent to indicate the cost of capital in Capital Transit.

MR. BEBCHICK: Excuse me, Dr. Limmer. Did you not mean D. C. Transit?

THE WITNESS: Yes.

[Page 1102, Line 22 - Page 1106, Line 10]

By Mr. Spear:

Q Dr. Limmer, I believe you were asked by your counsel whether conditions now warrant a shift to the operating ratio and you testified at Page 995: "There are no conditions which now warrant such a shift." Do you remember that testimony?

A [Dr. Limmer] Yes; I have it here.

Q Are you aware, sir, or do you have any views -- Let me change that. What is your view of what Congress meant by the word "conditions" in Paragraph 4 where it talks about shifting to an operating ratio?

MR. GOODMAN: I object. That calls for a statutory construction by the witness and he is not on the stand for that purpose.

CHAIRMAN HAYES: I think he has answered it by saying that there are no conditions which warrant it, in any event.

By Mr. Spear:

Q Let me put a preliminary question to you because you may not even know what I am asking you -- I think you may not. Are you aware, sir, that in Section 4 of the franchise Congress said, and I will read two sentences which are as follows:

"It is hereby declared as a matter of legislative policy that in order to assure the Washington Metropolitan Area of an adequate transportation system operating as a private enterprise, the Corporation, in accordance with standards and rules prescribed by the Commission, should be afforded the opportunity of earning such return as to make the Corporation an attractive investment to private investors. As an incident thereto the Congress finds that the opportunity to earn a return of at least six and one-half per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on either the system rate base or on gross operating revenues would not be unreasonable, and that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible and as conditions warrant" --

And I now quote the part that I believe is applicable to my previous question: "--that the Commission should encourage and facilitate the shifting to such gross operating revenue base as promptly as possible and as conditions warrant; and if conditions warrant not later than August 15, 1958."

You were aware, before I read this, of those provisions, were you?                   A     Yes.

\*       \*       \*

CHAIRMAN HAYES: Just a moment. I would like to ask a question before you proceed. You now say that you considered the question to be "Is it proper to shift", and your answer would be to that question "No", that it is not proper. Is that right?

THE WITNESS: That is right.

CHAIRMAN HAYES: Does that mean it is never proper under any condition -- under no condition would it be warranted?

THE WITNESS: In my view, Mr. Chairman, yes.

[Page 1114, Line 10 - Page 1115, Line 12]

By Mr. Spear:

Q   Now will you look back to Page 973 and tell me what you meant in Line 3 by the words "additional revenue"? You say, "To the extent that the company is able to contract expenses, there is additional revenue made available to cover fixed charges." What is the additional revenue?

A [Dr. Limmer] Perhaps a more accurate thing would be income. In other words, my point is that if expenses decline as revenues decline there is not necessarily a reduction in net income.

Q What do you mean by additional revenue? You didn't say there is the same amount of revenue, or revenue is unchanged. You say, "To the extent the company is able to contract expenses, there is additional revenue." Is that inaccurate?

A I am afraid it is not very clear and I would like to clarify that point. What I meant was that the income is not necessarily reduced and consequently the same amount of income may still be available to cover fixed charges even though there is a reduction of gross revenue.

[Page 1131, Line 13 - Page 1145, Line 24]

By Mr. Donnell:

Q Dr. Limmer, I have just a few questions, if you will. At Page 968 you state that you analyzed 11 local transit companies to obtain a cost of equity to apply to D. C. Transit. You state you chose those because they were comparable, in general, with D. C. Transit. Are those the companies listed on Page 2 of Exhibit Number 43?

A [Dr. Limmer] Yes.

Q And that is subject, of course, to the two that you have added this morning. I believe you said that this

list as amended this morning includes every transit company operating in the United States with the same characteristics as D. C. Transit.

A For which data are available in Moody's 1959 Transportation Manual, which includes all companies of invested interests, to the best way in which -- to the extent that Moody's get information from such companies.

Q Are you familiar with the Pittsburgh Railway operation or the Philadelphia transit operation, sir?

A I am.

Q You did not, however, include those?

A I did not include those for the following reasons: Philadelphia had losses for a number of years. That is why -- May I refer to my notes?

Q Yes, certainly.

A The Philadelphia company has had losses or no profits in five of the seven years between 1952 and '58. And if you count those negative ratios as zeros, the average for the period would be 1.3 per cent. I felt in view of the fact that there were so many losses it is not possible to obtain from the Philadelphia company a property valuation of what it would cost the D. C. Transit to obtain capital. With respect to the Pittsburgh company, the same situation obtained. It had losses in three of the seven-year period. I did not count it for the same reason.

Q In other words, the fluctuations of the transit industry don't always lend themselves to making a comparable exhibit to apply to another, is that right? In other words, you have excluded these because of the departure from norm.

A I didn't get the last word.

Q Departure from norm, normal.

A And the great departure from what would apply to D. C. Transit, which is a much more profitable company with a much better future.

Q Doctor, what do you mean when you say you analyzed a local transit company?

A I have examined the figures in its operations, revenues, traffic, income, dividends. stock prices. for a number of years.

Q You would in the first instance find out whether it was or was not a local transit company, would you not?

A Certainly.

Q We have already established that the National City Lines is a holding company, have we not?

A Yes.

Q I believe in your cross examination by Mr. Spear you so testified.

A That is correct.

Q Let's take the last company on the original list before the addition of two this morning. Does your analysis of the United Transit Company of Delaware show it to be a local transit company, sir?



A Well, it also is a holding company with subsidiaries operating in Virginia, particularly Richmond, Norfolk and Portsmouth; Tennessee, Nashville and Chattanooga; Illinois, Springfield,; Louisiana, Baton Rouge; Ohio, Akron and Youngstown.

Q Did you also find out, sir, that four of the 13 subsidiaries of this holding company are truck repair maintenance companies?

A As a matter of fact, the predominant part of its operations -- may I inspect my notes? The predominant part of its operations, as far as I can determine, are transit.

Q But nevertheless it is a holding company and not a local transit?

A That is right. I included it because I wanted to get, frankly, as large a number of companies of approximately the same size with predominantly transit operations, although other operations may be included -- may be in there on a minority extent.

Q Are any of the cities in which United Transit Company owns transit facilities comparable to the District of Columbia?

A In size?

Q Yes.

A Youngstown is the biggest city that it operates in and it had in 1950 -- that is, the metropolitan area of

is leased to the subsidiary, the Key System Transit Line, which operates a transit system.

Q As a fact, doesn't Moody's say it owns, rents and sells real and personal property?

A Yes, but if you look more carefully you will see that that property is leased predominantly to the Key System Transit Company.

Q Are you aware of the fact that it has nine employees?

A How many?

Q Nine.

A Bay Area?

Q We are talking about local transit companies which are listed on Exhibit Number 43, Page 2, I believe, sir.

A You mean the Railway Equipment Company has nine employees?

Q That is right, sir.

A Well, as a matter of fact it had -- that is the holding company itself. The whole system is such with subsidiaries -- it had total revenues in 1958 of \$10,800,000, which was somewhat less than it was back in 1952 of 13-1/2 million dollars -- \$10.8 million, which was less than it was for the years past, 1952 being as high as \$13.5 million. The revenue passengers in 1957, which are the latest figures I have, were 50,000,000 passengers.

Consequently, you see, I consider it primarily a transit operation and its income was that. That is, its

income from the public. The holding company itself had a few companies but its subsidiaries, of course, had many more.

Q You spoke about the National City Lines and we agreed that that is a holding company. A That is right.

Q Are you aware of the fact, sir, that it owns 67 per cent of the Railway Equipment and Realty Company and controls that company?

A I noticed that when I was looking through these.

Q And that it owns 49 plus per cent of the St. Louis Public Service Company, which is also listed here?

A Well, I noticed those facts. I don't have them at hand. I will accept them subject to check. There is a certain amount of interlocking relationship among these various companies.

Q That would also be true of the Baltimore Transit Company and the Philadelphia Transportation Company, would it not, sir? A What would be true?

Q That National City Lines owns a controlling interest in those operations.

A Well, I don't have the precise facts at hand. I know there is something like that.

Q I note, Doctor, that while you excluded from consideration the experience of Transit Company during the time that they had a strike, you made no similar provision with

reference to Baltimore in 1956 when they had a strike. Would you explain why you did not also exclude that figure?

A Frankly, I didn't know about it. I am willing to adjust the figures to take that into consideration.

Q I believe it was your testimony that earnings price ratios give a fair measure of market evaluation. Wasn't that your testimony, sir?

A It was.

Q I believe you also stated that that is true for electric and gas companies.

A Yes.

Q Isn't the reason that that is true, sir, for electric and gas companies, or one of the reasons, that they have fairly uniform earnings and dividends from year to year? Isn't that one of the reasons why it gives a market value?

A No, I don't think so. I would say that if a sufficiently long period is taken, such as I took over here, that it would be equally valid for these figures as it is for the --

Q I am going to come to that, sir, but I mean isn't that a reason why gas and electric companies --they have fairly uniform earnings--

A No, it is not.

Q It is not?

A No.

Q Isn't it a fact that that is true?

A That they have relatively uniform earnings?

Q That is correct.

A Yes, it is.

Q And in most cases have comparable capital structures. I am speaking now of the gas and electric utilities in general.

A I am not very familiar with the gas and electric companies.

Q Do you know whether or not electric and gas utilities usually have a uniform pay-out ratio?

A I don't have the figures in mind.

Q Looking at Page 2 of Exhibit Number 43, Dr. Limmer, isn't there a wide variation in earnings price ratios? In other words, they extend from zero to 31.8, I believe, from a quick scan.

A There is a variation, a wide variation from the lowest to the highest among the various companies that I have, but if you will notice from year to year, if you average the companies the variation is much less, including the two companies that I have. The lowest year that I have any figure for is '56, which is 7.40. The highest one is '53, which is 15.07. That to my mind is a relatively minor variation.

Q Do you think that there is any consistent relationship between earnings and market price in the transit companies which you have listed, sir?

A You mean from company to company or from year to year? What precisely do you have in mind?

Q Well, let's take Kansas City Public Service Company for the moment. I will give you the price range of the stock of that company for the years which you have listed here in the price earnings ratio. Or do you have them, sir?

A I have them.

Q May I either state them subject to check or have you read those into the record, sir?

A Why don't you read them?

Q I will do that. Will you take them subject to check? Nineteen fifty-two, one and three-quarters to three and one-quarter. Nineteen fifty-three, two and five-eighths to four and seven-eighths.

Nineteen fifty-four, two and seven-eighths to five and a quarter. Nineteen fifty-five, four and one-eighth to five and seven-eighths.

Nineteen fifty-six, three and a quarter to six and three-eighths. Nineteen fifty-seven, two and a quarter to four and a quarter. Nineteen fifty-eight, two and a quarter to five and three-quarters.

A The figures are correct, by the way.

Q Thank you. We have already listed, of course, the price earnings ratio. Does that demonstrate to you that there is any consistent relationship between earnings and market price for that particular company?

A The variability of the Kansas City Public Service Company is substantial. I have made an analysis of this for the various companies that I have. The Kansas City Company, by the way, is the smallest company I have, or one of the smallest. In 1958 it had revenues of 8.9 million dollars, which was somewhat less than it had in previous years. In '52 it had 13 million. It is also not listed.



The stock of the Kansas City Company is not listed, and my check over here indicates that companies having stocks which are not listed in organized exchanges have wider variability and earnings price ratio than those which are listed. It is true that there is quite a variability there and the Kansas City Public Service Company has, as you can see, a relatively high average, 13.43. I will say this: That it might be possible or you could argue that perhaps this analysis should be confined to larger companies, perhaps over 20 million of revenue, and with stocks on organized exchanges. My calculations indicate that this would give a substantially lower earnings price ratio than is indicated over here.

CHAIRMAN HAYES: You said 15.4, I believe, Doctor. I take it you meant 13.4.

THE WITNESS: If so, I misstated it.

By Mr. Donnelly:

Q Somewhere in your testimony I believe you indicated that dividends have something to do with the fixing of the market price, did you not?

A If I did not, I will say so now.

Q Are you aware of the fact that Kansas City, in spite of its wide variation in price earnings ratio, at no time during the interval we have covered has paid one red cent of dividends?

A I have the figures for three years and that is probably true for the entire period. Let me see. I think I have them for the entire period. Yes; that is true. No dividends at all. In other words, I am sure that the investors take that into consideration in earnings price ratio, which is one of the reasons for its high level.

Q Don't you believe that the capital structure of any given company is important, sir, in analyzing?

A It is a factor and that I am sure is considered by investors in the way they price the stock.

Q What consideration, if any, have you given to the capital structures of the companies which you have listed on Exhibit Number 43?

A I have given no more consideration than what the investors give in their pricing of the stock. It is my belief -- I think it is a very rational one -- that investors give full consideration to all the factors.

There are unique situations in every company, as I indicated before. Investors take that into consideration. Maybe they don't do it properly, but that is, to my mind the consideration that should be given in determining the return on capital under the capital cost method. To what extent investors give consideration to dividends, to what extent investors give consideration to differences in capital structure, would be reflected in the market prices.

That is the only thing that to my mind should be considered in fixing the return on capital, because that is what determines the cost of capital to a company in issuing securities, particularly equity.

Q You made a statement on 973 of the record that the average return on equity of 26 leading traction and bus companies for 1958 was 4.4 per cent. Do you believe a return of that nature is conducive to being able to raise capital, Doctor?

A I certainly do not. That is why I am recommending here a considerably higher one. In other words, I am not taking here the return on what the -- what these various bus lines are getting. What I am doing is to use a ratio that expresses the investors' capitalization of these earnings. How they evaluate these earnings as determined by their prices. Consequently, I am recommending, as you can see, a capital attracting rate of 11.16 plus an acquisition rate, which gives you a figure much higher than the 12 per cent.

Q Which is your judgment of what is necessary to attract capital in the case of D. C. Transit?

A It is not my judgment. It is the result of the investors' judgment, because all I have done here is to average the figures derived from a comparison of earnings with the prices. That is all I have done. That is the investors' judgement that has determined this figure. not mine.

[Page 1151, Line 3 - Page 1152, Line 22]

By Mr. Donnelly:

Q I have a few more questions. Would you turn to your Exhibit Number 43 at Page 3, Dr. Limmer, which is entitled "Current Earning-Price Ratio, D. C. Transit System, Inc." As I understand it, sir, you there took and divided the net operating income of the company as reported for the 12 months ending November 30, 1959 into the outstanding 2,500,000 shares or -- divided it by 2,500,000 shares of common stock of the Delaware parent company, is that correct?

A [Dr. Limmer] Yes.

Q Are you aware, sir, that there are two classes of stock in that 2,500,000?

A I am.

Q And are you aware, sir, that 500,000 are entitled to preferential dividend of one dollar before any dividends to the Class B stock?

A I am.

Q Would it not have been proper, then, sir, to get a current price-earnings ratio or to have divided your earnings per share -- to have divided the net income into the 500,000 shares of Class A stock, at least to the extent of the dollar per share earnings?

A Well, that is a controversial question. I think the argument could be made on your side and on the other hand, an argument could be made equally the other way.

Q What about this net operating income of \$892,765.  
It is before interest, is it not, Doctor?

A Before interest -- I don't have the figures in front  
of me right now.

Q In other words, it is the net operating income  
before interest, just as you say -- that is the net operating  
income, is it not?

A Yes, that is right.

Q Is it proper to divide that rather than after  
payment of interest?

A No; it isn't.

CHAIRMAN HAYES: I didn't get which way the answer  
"no" was intended to apply.

THE WITNESS: No, it isn't proper. The interest --  
it should be deducted before getting the earnings for the  
shares. May I point out that if this were done the figures  
would, of course, be much lower than they are now.

[Page 1170, Lines 13-23]

Q [By Mr. Spear] Have you ever testified in any rate  
proceeding relating to the fixing of any rate schedule in  
transit matters before this case?

A [By Mr. Limmer] I have not.

Q Have you ever made any study of the particular  
problems of determining what is a fair rate of return for  
the transit industry as distinguished from all other  
industries -- separately from all other industries?

A Previous?

Q Previous to this hearing. A No, I haven't.

[Page 1171, Line 20,- Page 1172, Line 20]

COMMISSIONER KERTZ: And I believe you testified that the earnings-price ratio is the proper measure to ascertain the cost of equity?

THE WITNESS: [Dr. Limmer] Yes, sir.

COMMISSIONER KERTZ: Is that your testimony?

THE WITNESS: Yes, sir.

COMMISSIONER KERTZ: Do you say further that the earnings-price ratio is the appropriate measure to test the cost of equity in the absence of any evidence as to what the market price of the stock is?

THE WITNESS: Well, in cases where a company has stock which is not widely traded, for example has no price, then it is proper and there is substantial precedent for it, to obtain earnings-price ratio of similar companies which have stocks which are traded and for which prices are quoted and available.

COMMISSIONER KERTZ: And your cost of equity determination here is based not upon the earnings-price ratio of D. C. Transit, but upon the earnings-price ratio of allegedly comparable companies. That is the sum and substance of your case, is it not?

THE WITNESS: Yes, sir.

COMMISSIONER KERTZ? That is all I have.



THE WITNESS: Except, I say one thing: We did include the parent company, D. C. Transit, for the few years' data where available.

[Page 1175, Lines 6-18]

Q [Mr. Goodman] Now when you testify that conditions did not warrant a shift to gross operating revenues as a basis for determination of fair earnings -- was that information or opinion based on economic considerations?

A [Dr. Limmer] It was, completely.

Q You were speaking as an economist, then?

A Yes.

Q Were you attempting to interpret the statutory language?

A No, I wasn't.

Q But in your opinion there is no economic condition which warrants a shift to operating ratio?

A That is right.

[Page 1189, Line 10 - Page 1198, Line 24]

By Mr. Bebachick:

Q Turning to Exhibit 51A, would you explain the changes that you have made therein and the reason for those changes?

A [Mr. Harris] Yes. The revision made therein, in Exhibit 51A, as compared to Exhibit 51, was the reversal of several income tax credits that D. C. Transit has

realized from August 15, 1956 through September 30, 1959. as the result of claiming as tax deduction track removal provision of \$1,044,196 per annum and that tax reversal has been made by deducting that amount from the gross remainder of the reserve provisions on the books of D.C. Transit at September 30, 1959, after taking, after the deduction of the undepreciated cost of their rail properties at that time of \$5,121,644. That is, I have deducted \$1,696,818 from the reserve provisions and come down to a net remainder available on the books of the company at September 30, 1959 for track removal and repaving of \$3,505,915.

Q You then, as I take it, reduce the reserve available for track removal and repaving and disposition of rail properties by an amount which represents an amount of effective taxes claimed due to the fact that the three million dollars or a little over three million dollars has been claimed by the company since 1956 as a deduction for income tax purposes -- that is to say, the amount that they have credited annually to the reserve for track removal and repaving, is that correct?

A That is correct.

Q So that the taxes in that amount really are no longer available for the reserve and the reserve realistically has to be reduced?

A That is correct.

Q What would be the effect, Mr. Harris, if the Internal Revenue Service were to disallow the claimed deductions taken by the company after credit to the reserve for track removal and if they were to incur an additional income tax liability in the future -- would this adjustment that you have made here take care of it or take that into account?

A Yes, sir, that would perfectly reflect such action by the Internal Revenue Service and then, of course, the company -- the basis for any such action by the Internal Revenue Service would be that this does not constitute an allowable deduction and that any such deductions must be based on actual expenditures for track removal and repaving. Of course, if they reviewed their income tax returns and disallowed that, this adjustment would perfectly reflect that. That is, the entries at that time on the books of the company would be to adapt this as a reserve provision and to credit the taxes payable, subject to their later expenditure, on materials, labor, and so on less salvage for the actual removal of the tracks and repaving.

Q So this adjustment, in effect, washes out or removes from relevant consideration what the company has done in the past with regard to charges for the track removal and paving account and these are the net figures from which we can proceed from this time forward?

A That is correct.

Q Can you then proceed, Mr. Harris, to explain the calculations on this exhibit?

A Yes, sir. I might clarify it at this point, what the \$3,505,915 item is. It is arrived at by adding the reserve provisions on the books of D. C. Transit as of September 30, 1959, of \$3,216,286, constituting the reserve for track removal and repaving and a balance of \$7,108,091 representing the unamortized balance of the original acquisition adjustment of \$10,339,041.

These two reserve provisions total \$10,324,377. From that I have deducted the full undepreciated cost of rail properties as of September 30, 1959, in the amount of \$5,121,644, and then I have further deducted the accumulated income tax credit of \$1,696,818, arriving at the remaining provision of \$3,505,915.

At the bottom of Exhibit 51-A I show a computation of the eventual reserve provision that should be accrued on the books of the company. That is constructed by adopting the Commission's accepted valuation of their track removal and repaving liability at \$10,441,960 and deducting therefrom the total income tax credits that will be realizable on the District tax and the Maryland tax, as well as the federal tax, amounting to a composite credit rate of 54.3148 per cent, resulting in a total income tax credit deduction of \$5,671,530.

MR. BEBCHICK: At this point, I would like to call the Commission's attention to an error. After the 5, it should be a comma instead of 5.671, where it says deduct income taxes.

By Mr. Bebachick:

Q Mr. Harris, you have just stated that as \$5,671,000?

A Yes, sir.

CHAIRMAN HAYES: This appears to be a period and it should be a comma?

MR. BEBCHICK: That is right.

THE WITNESS: After that deduction, we arrive at the net reserve provision required of \$4,770,430. Deducting from that \$4,770,430 the \$3,505,915 that is already or was already available on the books of the company as at September 30, 1959, of \$3,500,915, leaves an additional net reserve accrual necessary over the period October 1, 1959, to August 15, 1966, of \$1,264,515.

By Mr. Bebachick:

Q Mr. Harris, could you briefly tell us at this point -- or if you would care, when you discuss Exhibit 54-A -- how you make provision for this \$1,264,000?

A I make the provision on Exhibit 54-A, which I will leave until that time.

Q Do you have any other comments on Exhibit 51-A before we move to Exhibit 54-A, Mr. Harris?

A No, sir; I have stated it in the record. The transcript will show my position and it is unchanged.

Q Referring, then, to Exhibit 54-A, could you describe the changes that you made that exist in this exhibit, compared with Exhibit 54 which you explained last week?

A In Exhibit 54-A I have made two changes of substance which are reflected under the column headed "Adjustments" as items C and D. Item C is explained, the nature of that adjustment and the amount of it, on Page 2, under Note C. That explanation is that this adjustment is necessary to reverse the reserve provision of \$1,544,196 for track removal and repaving as it appears in the PUC staff projection for 1960 and to enter in lieu thereof a net reserve provision of \$183,929 for 1960, which is in accordance with Exhibit 51-A.

Referring back to Exhibit 51-A, I have just shown that the additional net reserve accrual required from October 1, 1959 through August 14, 1966 is \$1,264,515, which amounts to an annual net reserve provision of \$183,929 when divided by the 82-1/2 months remaining time.

This net provision is equivalent to a gross track removal and repaving expense provision of \$402,601, less an income tax credit of \$218,672.

The second adjustment that I have made to the original exhibit, Exhibit 54, is the adjustment of bus depreciation expense in the amount of a credit adjustment of



\$246,253. This adjustment item, which is denoted D, is also explained on Page 2 of Exhibit 54-A.

This note shows that the purpose of this adjustment is to adjust bus depreciation as shown in the PUC staff projection to reflect the removal from the depreciation base of the original cost of fully depreciated buses to be operated in 1960. Of these fully depreciated buses, there will be 371 in use from January 1, through April 30, 1960, with an original cost of \$4,066,344. Three hundred one of these buses will be retained in service from May 1, 1960 through December 31, 1960, with an original cost of \$3,243,655.

In this footnote, I have indicated the method of computing the depreciation adjustment and I arrived at the total credit adjustment of \$246,253 by taking account of the four months' operation with the 371 buses and eight months' operation with the 301 remaining buses.

Q Thus, Mr. Harris, you have, have you not, reduced the staff's objective figure for bus depreciation by the amount of buses which will be in use in 1960 which have already been fully depreciated; is that correct?

A Yes, sir.

Q I believe you stated last week in the transcript, starting at Pages 1054 and 1055 -- you there indicated, did you not, that the depreciation figure of the staff

was overstated in that it included depreciation on buses which already had been fully depreciated?

A Yes, sir.

Q And at that time you did not make an adjustment because, as I understand it, you did not at that time have available to you the figures which enabled you to make the adjustments reflected in Exhibit 54-A; is that correct?

A That is correct.

Q One further question, Mr. Harris. Have you made any changes not reflected on these two exhibits? Has there been any change made in the rate base as a result of your restudy of the situation since the original exhibits were given to the Commission?

A Yes, sir. I believe in my original testimony I indicated that I was using the rate base net investment in the rate base properties at September 15, 1959.

Q Will you refer, or are you referring now, to Exhibit 52?

A Yes, sir. I believe I testified that I was using the net investment in rate base property as of that date after deducting the undepreciated cost of rail properties at that date of \$5,121,644 in accordance with my position taken in Exhibit 51, and that I arrived at a net investment in rate base property of \$12,541,217.

I further explained that I had not attempted to arrive at a weighted average rate base over the year 1960 because the depreciation accruals from September 30, 1959 through December 31, 1960 would closely approximate the total original cost of the new buses to be added during the 15-month period.

However, in view of my adjustment of bus depreciation in Exhibit 54-A, which will bring the total adjusted depreciation for 1960 down to \$1,245,000, I would wish to modify my original testimony.

Q Your original testimony concerning the valuation of the rate base; is that right?

A Yes.

Q Will you please tell the Commission how you would adjust it?

A I have arrived at an adjustment in this fashion, to my Exhibit 52, rate base property computation. The total cost of the new buses to be added during the period September 30, 1959 through December 31, 1960 is indicated to be \$2,760,000. The total annual depreciation of my adjusted basis is \$1,245,000.

Allowing for the 15-month period that adjusted depreciation increases to \$1,556,000, which figure I deduct from the \$2,760,000, arriving at a net increase in rate base properties at December 31, 1960 of \$1,204,000.

Using the September 30, 1959 balance of \$12,041,000 and the revised December 31, 1960 balance sheet and dividing by two, I come to a revised rate base property value of \$12,643,000.

Q So then you would modify Exhibit 52 so that the final figure of net investment in rate base property would read, as I understand it, \$12,643,000; is that correct?

A Yes, sir.

Q What you then have done, as I understand it, is to include in the rate base the value of the buses to be acquired in 1960 to compensate for the fact that the bus depreciation is being reduced by adjustments you indicated on Exhibit 54-A; is that correct?

A Not exactly. I have taken account of the addition of the new buses and the offsetting effect of the revised depreciation expense.

[Page 1209, Line 19 - Page 1212, Line 25]

Q [Mr. Spear] Then is it your position that this ten million three included both the obligation to write off tracks and included the discount of rail property values that were carried in the net book value of 23-1/2 million dollars to Capital Transit, both items? Is that correct?

A [Mr. Harris] That is correct.

Q Well, sir, if that then represents the liability, as you testified at the top of 1034, it represents part

of the purchase price, in your theory, paid by D. C. Transit; correct?

A No, sir. As I testified there, it is not a part of the purchase price because here were these properties open for a bid. Here were the terms of this franchise. As a prudent purchaser, you would not pay a dime for the rail properties and you would take into account your liability to remove the tracks and repave.

Therefore, the terms of the franchise, in effect moved your purchase price bid down, that \$10,000,000. Of course, that was the best bid price that Capital Transit could get under the terms of the franchise conditions. In other words, Capital Transit could be said to have made an involuntary contribution of some \$10,000,000 in assets.

Q Sir, do I understand you then to be saying -- and I think you may not have understood my prior question -- that when the D. C. Transit acquired 23.8 million dollars of assets for 13.54 million dollars purchase price, that, in addition, it undertook an obligation or a liability incident with the franchise to remove the tracks? Is that correct? In addition to the purchase price it undertook that liability? Is that your position, sir?

A Yes; and they received the assets from Capital Transit. That is, the purchasers are not out of pocket because they assumed the liability.

They got a donation of so much in these assets, because the asset value was -- the purchase price was deflated to the extent of the liability assumed and also deflated to the extent that they showed remaining book values on rail properties. So, you have not paid in \$10,339,000. You are free and clear of your -- you are fully protected in the liability that you assume because you get assets to cover that liability.

Q Now, sir, is it then your testimony that because D. C. Transit undertook to convert and thereupon to remove tracks at the time it accepted the franchise, that the cost of track removal should not be charged to the public as part of the fare? Is that your testimony?

A Yes, sir, because the new owner does not pay for any such track removal and repaving. The asset value of Capital Transit was deflated in the purchase price to fully take care of your liability.

Q And that is why he bought 23.8 million dollars of assets for a 13.5 million purchase price; is that correct?

A Yes, sir.

Q If, then, he undertook a liability for the 10 million dollars of track removal cost or whatever it was estimated to be at that time, then should not the cost of acquisition of the properties -- the purchase price, if you will, sir -- be in toto not just 13.5 million dollars paid to Capital Transit Company but 23.8 million



dollars or some figure approximating it representing what he will some day have to pay to remove those tracks plus what he paid Capital Transit Company? Should not that combined figure be the total cost of acquisition to the new company, D. C. Transit?

A No, sir, Mr. Spear, because of this reason: As I have explained, D. C. Transit has paid \$13,478,000 here. They were able to purchase the property at that value because of the conditions of the franchise which deflated the asset values of Capital Transit to the extent of \$10,339,000.

I have applied \$4,600,000 of that \$10,339,000 to the net provision for track removal and repaving. Only \$4,600,000. The balance applies back against the rail property values in the same fashion as the accrued depreciation against those rail properties. It is a reserve. It is a hole in those assets and washes out those assets.

Based on my opinion of this transaction, D. C. Transit, in effect, holds some \$4,600,000 in assets as trustee. They have assumed the liability for \$4,600,000 and they have got the assets of \$4,600,000, so they assume no liability except for what they are actually reimbursed and protected on.

[Page 1295, Line 16 - Page 1300, Line 24]

By Mr. Donnellia:

Q A basic one: Generally speaking, isn't an acquisition adjustment simply a measure of the excess of original cost over purchase price?

A [Mr. Harris] Yes, sir.

Q Or the converse could be true, could it not?

A Yes, sir.

Q Now, assume for the moment that the property accounts of D. C. Transit System, Inc. had been restated to the basis of purchase price, what would have happened to the so-called reserve or the acquisition adjustment which you say is now available to the company?

A Well, in that event, Mr. Donnellia, I think Mr. Flanagan's testimony that I put in in my Exhibit 51-A indicated that all of this acquisition adjustment applied against the rail properties.

In the event it had been applied against these property values and the new assets valued at their purchase price, there would have been no further depreciation of the rail properties involved and, of course, the company would then have to accrue, for the coverage of its liability, to remove the tracks and to repave.

Q I am not sure that I quite got my question over. Let me put it this way: If the property accounts of D. C. Transit had been restated on the basis of the

purchase price, depreciation for corporate purposes would have been based upon that purchase price, would they not?

A Yes, Mr. Donnellia. I just applied part of that adjustment to wipe off the rail values, that is, it goes down to how you would revalue the properties on the basis of the purchase price.

Q Again pursuing my question, I think you have agreed that if they were restated on the basis of the purchase price then the depreciation would have been on the purchase price and it would have followed, would it not, that then there would be no acquisition-adjustment account?

A Well, I'm getting -- I'm sticking to the actual transaction here rather than a hypothetical case, Mr. Donnellia, because we have testimony here that this whole \$10,000,000 applied against the rail properties. Now, when you revalue the assets and you attempt to apply \$10,000,000 against the rail properties, that value wasn't there. You have something left over. Now, you can't apply it against the buses. You can't apply it against the current assets. I would think it would reflect itself in a reserve provision.

Q I will just pass on. I believe I understood you to state that the rate payers have already born the burden of the loss in rail value and the cost of track removal and repaving. Did you not state that, sir?

A I believe you asked me that question, Mr. Donnellia, and I took another position, which I would like to modify again at this time. Of course, the depreciation on rail properties at an annual rate of about eight hundred and fourteen thousand was continued from August 15th, '56 through September 30th, 1959 and that that entered into the rate actions of the Commission.

Q I am going to quote from Page 1033 and ask if this is a correct evaluation of your testimony. Starting at Line 14, sir.

MR. GOODMAN: Excuse me, Mr. Donnellia. May we give this to the witness?

By Mr. Donnellia:

Q In fact, I will start at Line 10 -- and I quote:

"That is, this exhibit shows that the value of all the rail properties, that remaining value of \$5,121,000 and the necessary provision for the liability of track removal and repaving, has already been taken care of on the books of D. C. Transit, that the fare payers have already borne the burden of this loss in rail values and this cost of track removal and the repaving, and that no further recognition should be taken of rail property values in the property rate base."

Now, forgetting for a moment the provision for track removal, and let's speak solely of the acquisition

adjustment, have the fare payers paid anything for that, sir?

A No, sir, except to the extent that I indicated in rail depreciation.

Q I think you consider that a donation of the previous owner, do you not?

A Well, I think -- there has been some burden here, Mr. Donnelly, since August 15, '56, as reflected in the rail depreciation, but I think I changed my testimony later upon a question directed by yourself to the effect that: No; I was mistaken. The transit riders had borne none of this expense.

So, now I modify my picture: That it has entered into the rate-making process since August 15, 1956, to the extent of the rail depreciation.

Q And the undepreciated original cost of five million a hundred and twenty-one thousand-odd -- that was the net undepreciated cost as of December 31, 1959, was it not, sir?

A That was the remaining undepreciable value -- Let me correct that. That was the remaining value of the rail properties on the books subject to further depreciation at September 30, 1959.

Q And that was after the eight hundred thousand year depreciation taken up to that point?

A Yes, sir.

Q I believe it is your position -- I think you have stated it several times, but I just want to make sure that I am correct -- that the rail property had no value as of August 15th, 1956.

A That is, I have said that any purchaser of the property would have so valued it, Dr. Donnelly, except for any salvage value.

Q You have taken your approach simply on the basis of the purchaser, have you not, sir?

A No, sir. My whole position here is based on the balance sheet of September 30th, 1959 and the reserve provisions on the books of D. C. Transit at that date.

Now, everything before that date was just my thinking as to how this would apply back to August 15, '56, what the logic was in the original purchase price.

Q That is what bothers me, Mr. Harris. You have discussed what the purchaser might have or might not have had in his mind at that time, but have you taken into consideration what the seller, who is the other party to the transaction, might have had in his mind?

A Well, of course, I think it's rather unprofitable to explore back there, but, --

MR. BEBCHICK: Mr. Chairman, I might add it is somewhat irrelevant, is it not?



CHAIRMAN HAYES: That is all right. Let's hear the rest of his answer.

THE WITNESS: Of course, the seller was looking for the best possible offer, and that is the offer that he accepted, finally accepted.

[Page 1302, Line 13 - Page 1304, Line 12]

By Mr. Spear:

Q Mr. Harris, you made a statement in response to cross examination just now that you based some of your testimony on statements of Mr. Flanagan that the acquisition adjustment, all of the acquisition adjustment, I believe you said, referred to rail properties and then you said as you showed on your exhibit. Now, will you tell us more specifically where in this record or in any other record there has been any such statement by Mr. Flanagan?

A [Mr. Harris] Yes, sir. That was put in as Page 2 of Exhibit 51.

Q Would you show me where, sir, on Page 2 of Exhibit 51 or 51-A?

A. Yes, sir.

Q Will you read me on Exhibit 51-A, Page 2, or 51, Page 2, where Mr. Flanagan says that the acquisition adjustment all related to rail properties?

A Starting on Line 11, Mr. Flanagan stated,

"That the consideration included also the obligation, accepted by D. C. Transit System, Inc., to

convert from streetcar operation to bus operation, to remove the streetcar tracks and to repave the track area. This obligation could be and has been measured in terms of money."

Now, going on from here, Mr. Flanagan did also put in the opinion of Price Waterhouse -- that the difference we are discussing should be labeled as a reserve for track removal and repaving, and that the cost of such work should be charged against this reserve as the work was done.

Q Where, sir, in any of the lines you have just read did Mr. Flanagan say, as you stated earlier today, that the acquisition adjustment could be related to the loss in value of the rail properties?

A No, sir. I made an interpretation of Mr. Flanagan's testimony, and then, going back, of course, the entire \$10,339,000 was not necessary and was overly excessive to provide for the track removal and repaving inasmuch as the gross liability was estimated at \$10,000,000 and the prudent business man knows that he gets a tax credit on that expenditure and that a dollar of gross expenditure amounts only to 46 cents of actual expenditure.

Q Mr. Harris, about 20 minutes ago, in answer to a question to Mr. Donnelly, you stated that you predicated your exhibits on testimony of Mr. Flanagan which you quoted in effect as saying that all of the acquisition adjustment

was related to loss in value of rail properties. Where on Exhibit 51-A, Page 2, did Mr. Flanagan say that that acquisition adjustment was related to loss in value of rail properties?

A No, sir. I believe I have explained my position here. When I say, if you are quoting me correctly, that this entire amount was applicable to the rail properties, I, of course, break that sum down into the two components because the entire sum is not required if the estimate of track removal and repaving is a gross amount of \$10,000,000.

Q Then your position that Mr. Flanagan's testimony was that the acquisition adjustment was entirely related to rail properties, to loss of value and to cost of track removal, is your interpretation of Exhibit 51-A, Page 2, and Exhibit 51, Page 2, also; correct?

A Yes, sir. That was my interpretation I was forced to, under the circumstances.

Q But in so many words, he didn't say that, did he?

A. No, sir.

MR. SPEAR: Just a moment, Mr. Chairman. That is all, sir.

MR. DONNELLA: I have one more question.

CHAIRMAN HAYES: Yes, Mr. Donnell.

By Mr. Donnell:

Q Mr. Harris, do you know, sir, that the Commission did not accept either Mr. Flanagan's suggestion or the

suggestion of Price Waterhouse, the company accountants, which are referred to in the Exhibit 51-A, Page 2?

A Yes, sir. I'm familiar with that fact, Mr. Donnella.

[Page 1551, Lines 12-24]

By Mr. Spear:

Q Would you describe what the significance of Exhibit 59 is and how, if at all, it applies to the determinations currently being made on the books of D. C. Transit and in this proceeding?

A [Mr. Falk] Well, these were the depreciation rates by classes of property that were prescribed by the Commission to become effective July 1, 1953, and they are the rates that are presently being applied to the original cost of the property to arrive at depreciation on the basis of original cost prior to the offset of the amortization of the acquisition adjustment in the amount of slightly over one million dollars.

[Page 1564, Line 5 - Page 1566, Line 25;  
Page 1567, Lines 5-16]

Q [Mr. Spear] There is in that five million dollars a substantial amount of undepreciated cost of properties that have been converted over the period since August 1956, is there not, that is, cost that has not yet been

depreciated or amortized, but yet on properties which had been converted?

A [Mr. Falk] Well, there may be some in there that's related to that property, but there hasn't been any accrual of depreciation on the property that was retired in 1958 since that time.

Q That is just the point -- that in that five million dollars there are properties which have not been either depreciated or amortized in that period or time and which do represent undepreciated cost of rail properties, so that to apply a corresponding percentage to those properties one should more accurately use the 60 per cent figure rather than the 49.4 per cent figure, even under your theory?

A No; I don't agree to that. This determination was made as of September the 30th of the undepreciated value of the property as of September the 30th, 1959.

Q But you are comparing a percentage or you are multiplying the percentage by a figure that doesn't correspond in time or what is in it to the percentage comparison you are using?

The percentage is a percentage of conversion being effected on that date, January 3, 1960, whereas the amount of undepreciated cost includes not only properties which are being retired at that time, but properties which had been retired and which make up the

difference between 49.40 and 60 per cent, so that the proper figure to use, if you are going to use the \$5,121,000 figure, would be 60 per cent, would it not?

A Well, I think that that is a matter that would have to be considered in the over-all depreciation study that I have recommended should be made before there is any further adjustment for amortization of that extraordinary property loss.

The unrecovered depreciation as of September the 30th was determined by the company in the amount of \$5,121,000. I checked that and determined that that was a reasonable determination. Now, since that determination was made you have abandoned approximately 49.40 per cent of your property.

Q Well, sir, the 49.40 per cent figure is a comparison of what was in operation on January 3, 1960 with what was in operation, say, on January 2, 1960?

A That is correct; yes, sir.

Q Now, is it your position that the part of the rail property undepreciated cost in the \$5,121,000 figure, representing the conversion of equipment and rail properties in 1958 and 1959, may only be recovered at the end of conversion, after 1963, shall we say? Is that your position?

A Well, I say it could be compensated for in the next adjustment that might be made for abandonment of



property. In other words, there should be a determination, a depreciation determination, between now and the end of 1963 to determine what additional property loss there may be that hasn't been recovered.

Q Well, sir --

A Now, that may include some unrecovered cost on property that was abandoned in 1958. It may be that there are offsetting depreciation accruals, particularly on the over-age buses, which I pointed to as being one factor that might lead to a determination that the deficiency does not exist even in the amount that is shown by your Exhibit Number 10-A in the amount of five million dollars.

\* \* \*

Q Sir, in this entire proceeding we are making one assumption, are we not -- that the depreciation reserve, in the absence of a study, is being accepted as a proper statement of the reserve because, as I believe you have already testified, it might be that it is inadequate and it might be that it is too much, but it isn't known; therefore, is it not correct that it should be accepted as appropriate and applicable to this proceeding in the absence of further study?

A Well, I certainly agree that the book reserve should be accepted as the reserve for purposes of this proceeding.

[Page 1570, Lines 10-20]

Q [Mr. Spear] You will agree, sir, the property actually abandoned in 1958, rail property abandoned by reason of conversion in the year '58, for example, did have an ascertainable amount of unrecovered cost attached to it?

A [Mr. Falk] That's probably so, that there was some unrecovered cost attached to that property.

Q And no amount of that, no part of that, particular amount, whatever it be, is in the calculations at the bottom of Schedule 3 of Exhibit 39?

A Well, not on the basis of the percentage that I applied.

[Page 1583, Lines 10-23]

MR. BEBCHICK: Let's say a piece of property is worth \$10 and you are depreciating only eight dollars; you have only had eight dollars go into the reserve for depreciation. Now, when you retire by taking \$10 out the property account and \$10 out the reserve for depreciation, since only eight dollars had been accrued to that reserve for depreciation, you have two dollars; the reserve for depreciation is then two dollars less than it would have been had the full value of the property, ten units, been depreciated. Consequently, in a computation of the rate base, your net-investment figure would be plus two dollars?

THE WITNESS: [Mr. Falk] Well, your net-investment figure would be two dollars more than it would have been if the full amount of depreciation had been provided.

[Page 1591, Line 11 - Page 1592, Line 17]

Q [Mr. Bebachick] Let's say received total assets were 23 million dollars, of which approximately five million dollars was cash, for a 13 million dollar figure, did they not?

A [Mr. Falk] Received assets of 23 million dollars?

Q I believe that is roughly the figure.

A I don't know where that figure comes from.

Q 23.8. That is from Appendix 2 of the 1957 Motor Vehicle Fuel Tax case.

A I believe that is correct; yes..

Q If assets to the extent of 23 million dollars were received, and these assets consisted of at least five million dollars in cash -- were received for only 13 million dollars because of an estimated liability for track removal, repaving and writing off streetcar assets of 10 million dollars -- let's assume that just for the sake of assumption -- you therefore would have no need for an annual accrual, would you? You would have five million dollars in cash which initially, at least, would take care of a good deal of the cost of track removal?

A I think on your assumption, then, the -- you are assuming in that 23 million dollars that there is a set value of road and equipment in the amount of 18 million dollars?

Q That is right, assuming that to be the case.

A I say if you take the position that the liability for track removal was taken into consideration in the purchase, then the value assigned to road and equipment is 18 million dollars and the company would be entitled to recover 18 million dollars through depreciation in the future rather than the approximately eight million dollars which we are presently permitting them to recover as the purchase price of road and equipment.

[Page 1594, Line 12 - Page 1595, Line 24]

Q [Mr. Bebachick] In regard to bus properties which make up the bus property account, can you tell me if there are any properties that are retired from that account prior to 14 years of life of the buses and, if so -- in other words, the average age is 14 years. Do you have any prior to 14 years? If so, what are the circumstances surrounding these earlier retirements and approximately what are the amounts involved?

A [Mr. Falk] They would be very minor. There are a few buses that were retired by reason of accidents in the past prior to 14 years, but I think generally in the

last 10 years I don't recall of any appreciable number of buses retired prior to a 14-year life.

Q We do know that there is a significant number of buses which remain in the property account subsequent to 14 years which are not retired until 19 or 20 years and on which depreciation continues to accrue.

A Under our group method.

Q Therefore, would not the effect be that the actual rate of depreciation would be different from that prescribed by the Commission in its order of 1953 which has been marked here this afternoon?

A On the basis of latest information, there would be indication that the 14-year life may be too short.

Q I am just asking you as an actual practical matter: Is not the fact that, in effect, the buses are being depreciated for periods longer than 14 years and at a rate different from that prescribed by the Commission, taking the group as a whole, since you keep many in after 14 years and you take a few out before 14 years. Is not then the effect to produce a depreciable life greater than 14 years and a rate different from that prescribed by the Commission? Is that not the practical effect?

A That, I suppose, would be the effect of group depreciation when you confine it particularly to buses, but there may be other property.

Q I am speaking just of the bus property account right now. That would be the effect, would it not?

A Yes.

[Page 1598, Lines 1-25]

Q [Mr. Spear] Are you familiar with the market price of the stock in June and July of 1956 when the contract with D. C. Transit's parent, TCA Investing Corporation, was entered into?

A [Mr. Falk] It is my recollection that it was in the vicinity of \$13 or \$14 a share.

Q And the price that D. C. Transit paid for the assets was \$100,000 more than the contract price that had been agreed on a few weeks prior to D. C. Transit's -- I am sorry -- that had been agreed to by the date of D. C. Transit's offer between the board of Capital Transit Company and National City Lines, another company interested in the Capital Transit Company?

A That is my understanding, Mr. Spear. I wasn't present at any of those negotiations.

Q Weren't you furnished with a copy of the contract, sir, between National City Lines and Capital Transit?

A I may have seen that. I don't recall. I understand that Mr. Chalk upped his figure \$100,000.

Q And the actual price of \$13,440,000 offered by National City Lines to Capital Transit Company represented a figure which was precisely the market price of the stock at that time multiplied by the number of shares outstanding; is that correct?

A So I am advised.



[Page 1671, Line 1 - Page 1672, Line 11]

By Mr. Spear:

Q Mr. Flanagan, have you also reviewed and considered the testimony and exhibits presented by Mr. Harris?

A [Mr. Flanagan] Yes.

Q Would you comment on them?

A Yes. Referring to Exhibit Number 51-A, if this exhibit is to be given any weight, there would have to be some justification for Mr. Harris's assumption that the representatives of D. C. Transit System, being prudent men, consider the rail properties acquired from Capital Transit Company to have no value.

A few figures will demonstrate the fallacy upon which Exhibit Number 51-A is built.

The results of operations of the rail system since its acquisition by D. C. Transit System, Inc. are as follows:

In 1957 the gross-operating revenues derived from the operation of the rail system amounted to \$12,374, 563. The net-operating income, before income taxes, was \$1,780,619.

In 1958 the gross-operating revenues were \$11,842,712. The net-operating income, before income taxes, was \$1,438,285.

In 1959 the gross-operating revenues from the rail system were \$10,937,841 and the net

operating income, before taxes, was \$1,426,361.

I believe anyone will agree that a prudent man would be delighted to acquire such properties for nothing. However, in my opinion, to put it bluntly, any man who would give such property away should have his head examined.

As further proof of the value of the rail properties, a well-known bank was perfectly willing to lend D. C. Transit the sum of \$3,500,000 with rolling stock, which, of course, included streetcars, as collateral.

[Page 1674, Line 1 - Page 1675, Line 7;  
Page 1675, Line 16 - Page 1676, Line 12]

THE WITNESS: [Mr. Flanagan] In connection with that loan, I might comment banks are not noted for lending money upon worthless property. As the last comment, I would like to remind the Commissioners that I was a director of Capital Transit Company, that this entire transaction came before the directors for a vote, and I can assure all concerned that no director, to my knowledge, had any idea the streetcar property was worthless and that Capital Transit Company was not being paid for it.

By Mr. Spear:

Q Mr. Flanagan, will you comment on Exhibit 51-A and particularly on Page 2 of it?

A The Page 2 appears to be a portion of the testimony that I gave at some time or other. Mr. Harris testified that he read into my remarks my admission that the street-car property was worthless.

The language that I have used here is perfectly simple. Among other things, I said:

"The consideration included also the obligation, accepted by D. C. Transit System, Inc., to convert from streetcar operation to bus operation, to remove the streetcar tracks and to repave the track area. This obligation could be and has been measured in terms of money."

To me, that means exactly what I knew it meant to myself when I said it, and that is that D. C. Transit was assuming the obligation to tear up the tracks and repave the area, and it had absolutely nothing to do with the price being paid for street railway property.

\* \* \*

Q Mr. Flanagan, would you make reference now to Exhibit 54-A and give your comments on that exhibit?

A Again Exhibit Number 54-A has been built upon the premise that the representatives of D. C. Transit System, Inc. didn't pay anything for rail property that historically had provided all of the net-operating income for the predecessor company over many years and which property had seven years' life left, with potential net operating income that has actually been earned during only three years in the amount of \$4,500,000 and still has some time to go to earn more.

Of course, when Mr. Harris suggested treating depreciation accumulated on buses as a problem separate and apart, he admitted, as I remember it, that it was just his own idea and had not been adopted by other regulatory agencies which authorized group depreciation.

It is my opinion that the testimony I gave earlier today dealing with the history of the depreciation reserve of D. C. Transit System, Inc. has consistently demonstrated that the adoption of Mr. Harris's views would mean to disregard the rulings of this Commission over many years.

[Page 1692, Lines 11-25]

By Mr. Spiegel: [Addressed to Mr. Flanagan]

Q Do you know whether or not the parent company of D. C. Transit, the Delaware Company, or whether the grandparent company, Transportation Corporation of America, or any of the principal stockholders of Transportation Corporation of America have, in the last three years, borrowed money from Chase Manhattan Bank?

MR. SPEAR: Mr. Chairman, not only is this improper cross on the rebuttal, but it is even improper cross examination at any time. This has nothing to do with this proceeding.

COMMISSIONER KERTZ: I will go along with your first objection.

It seems to me, Mr. Spiegel, this is not proper examination.

[Page 1696, Line 3 - 1697, Line 3]

COMMISSIONER KERTZ: Mr. Spiegel, unless you are prepared to put on any testimony at this point, I will have to sustain the objection.

MR. SPIEGEL: Well, I am prepared to put on the evidence. The evidence is this witness. It is his knowledge. I am not on the inside of their operation, but it seems to me, as a public utility commission having regulation, having the witness before you, here is your opportunity to find the answer. It is something that we should have. Why should we run away from the question? Why should we run away from the facts?

MR. SPEAR: It has already been answered, Mr. Chairman.

MR. SPIEGEL: This question has not been answered.

MR. SPEAR: It has been answered.

MR. SPIEGEL: The question I asked as to whether or not there were loans from that bank, unsecured loans, has not been answered.

MR. SPEAR: You are asking the witness for knowledge outside of his knowledge.

MR. SPIEGEL: I think if he doesn't know he can answer that.

COMMISSIONER KERTZ: Mr. Spear, I have ruled on this. Let's proceed.

[Page 1738, Line 23 - Page 1739, Line 12]

Q [Mr. Spear] What conclusion do you derive from the figures shown on Exhibit 84 for purpose of selection of operating ratio and/or system rate basis for determining rates?

A [Mr. Curtin] I conclude that it is impractical and virtually impossible to properly safeguard public transportation requirements in the City of Washington, retaining a basis of rate making that departs from other utilities in the area as much as this does in this instance. Some greater measure of protection of the service to the public must be accorded and operating ratio is the appropriate measure to insure that protection.

Q Do you, sir, recommend that the operating ratio method for rate determination be used by this Commission in this proceeding?

A Yes, sir; I do.

[Page 1831, Line 16 - Page 1834, Line 1]

Q [Mr. Goodman] Six and one-half per cent is not needed to attract capital on favorable terms, is it?

A [Mr. Flanagan] It might be.

Q At this time

A We may be wrong. I cannot answer that categorically that it is not needed to attract capital.



Q What is the position of the company? Perhaps your counsel should state this. Are you urging a 3.86 profit margin in this proceeding or are you urging a 6-1/2 per cent profit?

A In this proceeding we are asking for a rate schedule which, as I pointed out, will give us certain rates of return under the gross operating ratio theory as shown on my Exhibits 13, 14 and 15.

MR. SPEAR: Mr. Chairman, counsel has asked company counsel's position. I will be glad to state it.

We believe we are entitled to a 93.5 ratio, which means 6-1/2 per cent. We believe that the law is clear that that is regarded as reasonable and will argue that in argument.

It is our position that based upon our computations of the results projected as we see them, we do not need more than what we are asking for. Of course, there is some difference in this proceeding as to what the computations are. In no event are we waiving our 6-1/2 per cent or the 93.5.

Based upon our figures, our computations as we see them, we don't at this time believe we will need any more. That is why we are not asking any more.

CHAIRMAN HAYES: I thought the witness had categorically answered by saying it was not needed.

MR. GOODMAN: Yes, and that is what troubles me, Mr. Chairman.

CHAIRMAN HAYES: All right.

By Mr. Goodman:

Q Mr. Flanagan, do you believe the company is entitled to a profit margin that is not needed to attract capital on favorable terms?

A I have not asked for a profit margin which is not needed. All I said, Mr. Goodman, was that Congress provides that we shall be granted the opportunity to earn 6-1/2 per cent. I have not asked for that opportunity today.

Q Then in your opinion, since you have quoted the statute, conditions do not now warrant a shift to operating ratio, do they?

MR. SPEAR: Mr. Chairman, there is no basis for a any -- I am sorry. I thought you were finished.

By Mr. Goodman:

Q Since you do not need the indicated return element?

A I don't know where you get that idea, Mr. Goodman. That is so far wide of the mark that it is ridiculous. I have said nothing of the sort. I have claimed from the very outset that we need and request and feel confident that we are entitled to authorization to adopt a gross operating ratio method now.

Q Do you believe that a reasonable operating ratio after taxes, for this Commission to use in this

proceeding, would be 93-1/2 per cent?

A I am not asking for it.

[Page 1868, Lines 4-16; Page 1870, Lines 3-4]

By Mr. Goodman:

Q Does the company plan to retire any buses in 1960 which are less than 14 years old?

A [Mr. Flanagan] It has no plans to at this time.

Q Does the company plan to retire at any time in the future buses which are less than 14 years old?

A Not so long as they are capable of being maintained in good, safe, operable condition; no.

Q And has the company at any time in the past retired such buses --

MR. SPEAR: Mr. Chairman --

MR. GOODMAN: -- with lives of less than 14 years except when there has been an occasional wrecked bus?

\* \* \*

THE WITNESS: No, unless they become inoperable through fire or accident.

[Page 1875, Lines 1-22; Page 1876, Line 12 - Page 1877, Line 1]

By Mr. Goodman:

Q This letter of January 19 to Mr. Norman Belt, signed by you, states, does it not, that you are making

a commitment to convert the four remaining rail lines -- those remaining after January 3rd, 1960, on the first Sunday in January, 1962?

A [Mr. Flanagan] Yes.

Q And when you say "this commitment is made with the following considerations in mind," and you state thereafter "We feel that we have demonstrated our full compliance with the provisions of Public Law 757 and with the interests of the Public Utilities Commission," does that last sentence condition the commitment of conversion that you earlier make with respect to the timing of your conversion program?

A I didn't say conditioned, did I?

Q Well, that is my question. What do you mean by it?

A I said it is a consideration, that we took this into consideration in making this commitment.

Q And your commitment is in no way conditioned by this argument?

A The letter is written in very plain English. I wrote it, Mr. Goodman.

\* \* \*

THE WITNESS: Mr. Goodman, we don't use double talk. If I were going to condition this commitment, I would have said "This will be done upon the following conditions". I didn't say that.

By Mr. Goodman:

Q I know you didn't say that. That is why I am asking my question.

Will the company, nevertheless, convert the remaining streetcar operations that remain after January 3, 1960, even though the Commission finds or should find that the company has not complied with the provisions of Public Law 757 and therefore should not obtain an operating ratio standard?

A The letter makes the commitment. There are no conditions attached to that.

[Page 1879, Line 2 - 1880, Line 6]

Q [Mr. Goodman] What track removal costs are to be incurred in 1960?

A [Mr. Flanagan] Will be incurred in 1960?

Q Yes. Have you any estimate?

A No. That is such an indeterminate factor --

Q You can't even estimate it for 1960?

A No.

Q What is your timetable for incurring costs of removing tracks? Have you any plans for the amount to be spent in any future period?

A Congress provides -- and this is what will govern, I believe -- that the corporation will go forward and gradually convert its street railway operations within seven years --

Q Excuse me, sir. I am not asking what Congress has provided.

A That is what is guiding us, and the District of Columbia. Congress enjoins upon us the duty of doing it when it is appropriate to the highway development plans of the District of Columbia and the economies implicit in coordinating the corporation's track removal program with such plans.

Q Therefore, you have no definite plans because you don't know what the Highway Department is going to do; isn't that true?

A That is right.

Q And, therefore, you don't know how much -- you can't plan how much will be spent in any particular period for track removal and repaving costs?

A I don't know how many times I have to say it. The answer is no; I cannot.

[Page 1929, Line 7 - 1930, Line 13]

By Mr. Goodman:

Q Now, you urge, I take it, a 93.5 per cent operating ratio after taxes?

A [Mr. Curtin] Yes.

Q And I take it you urge this 93.5 per cent operating ratio to provide a satisfactory margin for the company's operations?



A Yes.

Q What standards do you have for a satisfactory margin?

What comprises a satisfactory margin?

Why is one margin satisfactory and another not for a particular company?

A Well, this is an empirical derivation which, I have indicated in testimony, is derived from a series of sources. It represents what is the experience or a consideration, composite of several considerations, one being the experience of probably the most comparable system whose history can be reviewed over a long period of years, the Greyhound Corporation. It represents also the composite of the thinking of many commissions, knowledgeable people, who have studied this problem at considerable length and have made a determination in the basis -- in actual instances they have been confronted with.

There is a listing of some 20-odd commissions which have made decisions, commissions and other regulatory groups which have made decisions, in that general area presented here.

It represents also the findings of a comprehensive study of bus fares made by the Interstate Commerce Commission as a result of a several years' study made here about a decade ago.

[Page 1933, Line 15 - Page 1935, Line 3]

MR. GOODMAN: As I understand the witness's testimony, sir, he doesn't rely on any specific figure. All the figures he has put in are background considerations; but he doesn't rely on any specific figure which shows a 93.5 per cent operating ratio is reasonable for D. C. Transit.

CHAIRMAN HAYES: Well --

MR. GOODMAN: Is that true?

THE WITNESS: [Mr. Curtin] Eleven years ago I indicated that a figure of 85, on a range of 85 to 86, 87, averaging 86, which is equivalent to 93 and a fraction today.

Now, what you are asking me really is like asking a person -- I have been, as I indicated, working at this, various phases of it, for some 25 years -- it's like asking me: As a human being, what about eight hours' sleep? Do you believe in it or not?

Now, I haven't made any specific study about it, but eight hours' sleep to me is a reasonable night's sleep. There are some nights when you can get by on three or four, like some companies can bet by with half of what might be reasonable. They'll get by on it for a while, but it still doesn't alter the reasonableness of eight hours' sleep, and I don't think you have to make a specific study,

having worked in a field or working daily in a field for 25 years. I know this company. I have worked for this company on and off for a great many years, and I know the application of this company to a reasonable standard, which is industry-wide.

This is a local transit system in every sense of the word.

MR. GOODMAN: So you believe --

COMMISSIONER KERTZ: The answer is: You have not made a study with respect to this particular case; this is a matter of your judgment?

THE WITNESS: Yes; except this: I have made a study -- I have made continuing studies -- of the predecessor company to this. I have worked for them regularly, and I know the extent of an application of a general rule to this system.

[Page 1950, Line 19 - Page 1951, Line 24]

Q [Mr. Spear] Also, Mr. Curtin, would you refresh your recollection on the question asked you last Monday, the 15th of February? You were asked when you had been contacted for testimony in this proceeding. Was it not on Monday, February 8, in fact, that you got a call from me about appearing here as a rebuttal witness?

A [Mr. Curtin] That is right.

Q One week before you appeared?

A Yes.

Q That was the first call I made to you?

A The first time, I believe, I ever spoke to Mr. Spear was Monday, February 8.

Q Did I send you, sir, all of the transcripts, the complete set of transcripts, in this proceeding?

A I have the letter of transmittal

Q Do you remember getting the transcripts, too, sir?

A Yes.

Q And you got all the transcripts as of that date?

A That is correct.

Q Did you also get the exhibits with that transcript in the same package?

A That is correct.

Q Now, sir, one other thing: You were asked what you had done to acquaint yourself with circumstances and factors relating to the application of both GOR and, in particular, 93.5 to this case. I believe you indicated you made the various studies referred to in the exhibits.

In connection with making those recommendations, did you not also study the transcripts and exhibits in this case in addition to the other general knowledge you described?

A I believe I indicated that; yes.

[Page 824, Lines 10 - 22]

THE WITNESS: [ Mr. Falk ] On page 628 I was dealing with the question of the return to be provided D. C. Transit System, Inc., of the District of Columbia. That is the company we are interested in. The capital structure of the company has a very thin equity, but this Commission had no jurisdiction over that capital structure whether franchise was granted. What D. C. Transit System of Delaware does I don't believe we can control. The company applied to this Commission to split their stock and the company later withdrew their application.

By Mr. Spiegel:

Q And split the stock of the parent D. C. Transit of Delaware?

A We have no jurisdiction over that.

\* \* \*

[Page 825, Lines 3 - 14]

My question still is whether it is sound to use the test which you used on page 628 in the light of the kind of dealings and transactions in the capital once and twice removed from the company, as disclosed in Exhibits 41 and 42. Does this sound economical?

A What happens up there I don't think has one thing to do with what I have recommended in this case.

Q In other words, in setting the rate of return you would ignore the facts in Exhibits 41 and 42?

A I didn't ignore them. I didn't have them before me at the time. I didn't consider them because I was dealing with the D. C. Transit System of the District of Columbia.

[Page 928, Line 1 - Page 930, Line 11]

Q [ Mr. Spear ] Are you the same Colonel Roberts that entered an appearance in a rate proceeding before this Commission about a year and a half ago?

A Yes; I did, for Safeway Trails Company, of which I am part owner, a bus operation between here and Portland, Maine.

Q And Safeway Trails is a competitor of D. C. Transit in certain areas of operation?

A No.

Q It was at that time --

A In no legitimate operation; no.

Q It was a competitor of the D. C. Transit in the sightseeing and government-charter business; is that correct?

A In sightseeing and government charter, we definitely were affected by competition; yes.

Q And Safeway Trails has also intervened and opposed D. C. Transit's applications before the Interstate Commerce Commission for various authorities, including both government-contract service and limousine service to New York?

A That is correct; long-haul service and special service other than mass transportation in D. C.

Q And your firm represented them in those proceedings?



A Not only did I represent them, but I am a one-quarter owner, so I was interested personally.

Mr. Spear: Mr. Chairman, I am going to object to any opinion evidence on two grounds.

First, this witness is a prejudiced witness representing a competitor of D. C. Transit and does not speak as an expert with impartial views.

Secondly, he has not been shown to be an expert but just an attorney qualified eminently as an attorney but not as an expert witness on matters of economic judgment and rate-making procedures. However qualified he may be as an attorney and member of the bar, he is not qualified as an expert on matters of valuation of rate structures.

THE WITNESS: I think I ought to reply for myself to the effect that I only proposed to testify in the sense that I am a citizen of the District of Columbia and a resident of it and have been all my adult life. I have been associated with this company and often have been involved in matters in favor of the improvement of the transportation system, as often as I have in any restriction upon their activities.

There is no question about my interest in transportation systems. I represent many transportation systems. I also have represented states, cities and, most recently, the entire State of New Jersey and the counties and the

municipalities in New Jersey in matters affecting what amounts to suburban transit. I think my testimony could be qualified by the Commission.

I do have a financial interest in the sense that our company might do a little better on the sight-seeing operation and, of course, if D. C. Transit operations were conducted in common-carrier service to New York City they would be in direct competition, but we have no interest except their best health and the best operation as far as mass transportation is concerned. I have not been asked any questions as to my expertise.

[Page 865, Line 19 - Page 868, Line 1]

Q [Mr. Goodman] On page 633 of the transcript [JA 135], Mr. Falk, you mention that you include in your return allowance a cushion for increased cost which will occur after November 1st of 1960.

A [Mr. Falk] I think the return at the level that I have recommended does contain some cushion; yes.

Q Have you made any studies of the revenues that will be obtained by the company after November 1st, 1960 and beyond March 1st, 1961 -- the trend of traffic; the passengers carried; the amount of operating revenues the company will obtain?

A The figures in this case were all based on the calendar year 1960. We didn't go beyond 1960 in either estimating expenses or revenues.

Q You estimated the expenses to the extent or sufficiently for the purpose of including a premium for increased costs after November 1st, did you not?

A Well, I know for a fact there are going to be increased labor costs that become effect[ive] next November 1st that we only have in our calculations for a period of two months. I know for a fact under the contract they are going to be effective for the year 1961, but I haven't attempted to project expenses beyond 1960.

Q Well, those increased labot costs, effective November 1st, 1960, are reflected in the 12 months' income statement for 1960, aren't they?

A For two months, but they're not in there on a 12-month basis.

Q But they are effective for no longer than two months in 1960? A What is that?

Q But they are effective for no longer than two months in 1960, are they? A I say: But they'll be effective for the full year of 1961.

Q But you have made no estimate of the revenues that will be obtained in 1961 to see to what extent these costs will be offset in 1961, have you? A Well, we have, in estimating the effect of our fare structure here, assumed there will be no normal decline, that the transit fares will remain at the level they are -- I mean the transit revenues will remain at the level they are -- at the present time except for the resistance to the higher fares.

Q Through 1961; through March -- A Through 1960.

Q And you have made no study concerning 1961?

A No, sir, nor have I put in any other additional expenses beyond 1960.

Q What is the amount of this cushion that you include in the return allowance? A You can't measure it in exact dollars. I think the return that I have recommended, I believe, falls within the range of what is a reasonable return. Now, it may be near the top level of that range. I believe it does provide some cushion.

1. The first part of the report is a general introduction to the subject of the study.

2. The second part of the report is a detailed description of the methods used in the study.

3. The third part of the report is a detailed description of the results of the study.

4. The fourth part of the report is a detailed description of the conclusions of the study.

5. The fifth part of the report is a detailed description of the limitations of the study.

6. The sixth part of the report is a detailed description of the implications of the study.

7. The seventh part of the report is a detailed description of the future research.

8. The eighth part of the report is a detailed description of the references.

9. The ninth part of the report is a detailed description of the appendix.

10. The tenth part of the report is a detailed description of the index.

11. The eleventh part of the report is a detailed description of the bibliography.

12. The twelfth part of the report is a detailed description of the glossary.

13. The thirteenth part of the report is a detailed description of the list of figures.

14. The fourteenth part of the report is a detailed description of the list of tables.

15. The fifteenth part of the report is a detailed description of the list of abbreviations.

16. The sixteenth part of the report is a detailed description of the list of symbols.

17. The seventeenth part of the report is a detailed description of the list of acronyms.

18. The eighteenth part of the report is a detailed description of the list of initialisms.

19. The nineteenth part of the report is a detailed description of the list of contractions.

20. The twentieth part of the report is a detailed description of the list of colloquialisms.

21. The twenty-first part of the report is a detailed description of the list of idioms.

22. The twenty-second part of the report is a detailed description of the list of proverbs.

23. The twenty-third part of the report is a detailed description of the list of sayings.

24. The twenty-fourth part of the report is a detailed description of the list of maxims.

25. The twenty-fifth part of the report is a detailed description of the list of aphorisms.

26. The twenty-sixth part of the report is a detailed description of the list of epigrams.

27. The twenty-seventh part of the report is a detailed description of the list of epigrams.

28. The twenty-eighth part of the report is a detailed description of the list of epigrams.

29. The twenty-ninth part of the report is a detailed description of the list of epigrams.

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

United States Court of Appeals  
for the District of Columbia Circuit

FILED FEB 11 1963

Leonard N. Bebachick, et al.

Appellants

v.

Public Utilities Commission of  
the District of Columbia, et al.

Appellees

*Nathan J. Paulson*  
CLERK  
No. 16,454

APPELLANTS' MEMORANDUM IN SUPPORT  
OF PROPOSED JUDGMENT

Plaintiffs believe that the Court should enter the form of judgment attached hereto. This judgment provides for the most appropriate and equitable method of effectuating the Court's opinion of January 31, 1963.

I

THE ORDERS BELOW:

The Court has found that the reasonableness of the end result reached by the Commission is not supported by the record. Consequently, the judgment of the District Court should be reversed and the Order of the Commission should be set aside and vacated, without further proceedings except as may be necessary to effectuate appellants'



relief as decreed by this Court. Washington Gas Light Company v. Baker, 88 U.S. App. D.C. 115; 188 F2d 11 (1950).

## II

### THE REINSTATEMENT OF THE STATUS QUO ANTE

As no lawful basis exists for the Commission's Order promulgating a 25-cent cash fare, the Court should direct Transit to take appropriate steps to reinstate the prior existing lawful 20-cent cash fare. Transit may readily accomplish this by filing appropriate supplements or amendments to all tariff filings which became effective on or after March 6, 1960 and which set forth a 25-cent cash fare. These tariff supplements or amendments, cancelling the 25-cent cash fare and reinstating the 20-cent cash fare, should be ordered to become effective, nunc pro tunc, as of the effective date of the tariff filings thus supplemented or amended. These amendments or supplements would not otherwise interfere with any tariff filings which presently are effective. Nor would they in any fashion affect suspended tariff filings which are the subject of pending administrative proceedings.

The issuance of Commission Order No. 4735 of January 18, 1961, does not bar the Court from ordering the reinstatement of the prior 20-cent cash fare. Order No. 4735, while formally superseding Order No. 4631, here on

review, merely served to continue in effect the 25-cent cash fare and keep alive the controversy as to the legality of that increased fare. In issuing Order No. 4735, the Commission rejected an increase in the token fare subsequently requested by Transit. The reasonableness of the 25-cent cash fare per se, was not treated by the Commission as being in issue and was not the subject of an independent administrative determination.

Moreover, the Order and Opinion of the Commission (38 PUR 3rd 19) on its face make it clear that the Commission simply repeated each of the rate-making practices which the Court here has found are unlawful and constitute reversible error -- (a) depreciation was allowed on abandoned street rail properties in the absence of the inquiry and findings required by the Baker case; (b) depreciation on fully depreciated buses was allowed for six months of the future annual period; (c) the Commission allowed an annual \$1 million track removal and repaving accrual on the theory that all the tracks would be removed and the areas they had occupied repaved and, also, that Transit alone would be required to meet the total cost of such a program. In addition, the accrual again was accompanied with the vague promise of further study although the record clearly established that Transit had on hand an unexpended reserve for track removal and repaving considerably

in excess of its actual requirements through fiscal 1966. Thus, in reaching its decision here, the Court has found that no lawful basis can exist for Transit's continuing to charge District of Columbia transit riders a 25-cent cash fare.

### III

#### THE RELIEF TO BE GRANTED

Transit riders are entitled to receive restitution for the payment of unlawful fares. Capital Transit Company v. Public Utilities Commission, 93 U.S. App. D.C. 194; 213 F2d 176 (1953); Washington Gas Light Company v. Baker, 88 U.S. App. D.C. 115; 188 F2d 11 (1950); see appellants' Reply Brief, pp. 5-8. As it obviously is not possible to repay the unlawful 5-cent portion of the 25-cent cash fare to individual transit riders, the appropriate equitable remedy would be to make these sums available for the benefit of future transit riders as a class.

(a) It would be inequitable to appellants and the members of the transit riding public whose interests they represent to remand this proceeding to the regulatory body for another determination of the lawfulness of fares collected during the past three years. Transit has the burden of proof to establish evidence on the record demonstrating its need for increased fares. Enforcement of this burden is the consumers' only enduring protection against

excessive fares. To permit the Company to relitigate the reasonableness of past fares which the Court has found were unlawfully prescribed allows Transit to dispense with this standard of proof, thus bypassing the interests of consumers. cf. Washington Gas Light Company v. Baker, 90 U.S. App. D.C. 98, 104-105; 195 F2d 29, 35 (1951).

In the first Baker case, this Court ordered restitution of the unlawful fares collected in the past after finding the Commission's Order invalid because of the inadequacy of the record and findings with respect to certain operating expense accruals. That is precisely the situation here. No basis exists for departing from the type of relief granted consumers in Baker.

(b) Restitution can best be accomplished by requiring the Company to account for and fund the monies unlawfully collected which would be utilized for the benefit of transit riders as a class, such as absorbing future cost increases which otherwise would require fare increases or enabling the institution of fare reductions.

This fund should be in an amount equal to 20% (5/25) of the cash fares collected by Transit for transportation of passengers in the District of Columbia during the period March 6, 1960, to the effective date of the tariff supplements or amendments cancelling the 25-cent cash fare, inclusive. No lawful basis existed for the collection of a

25-cent cash fare during this entire period. This proceeding should be remanded to the District Court with directions to act as a court of equity and to take all steps necessary to implement a decree of restitution and to create a fund for the benefit of transit riders.

Once vested with jurisdiction to award equitable relief, the District Court possesses the full scope of the historic power of equity to provide for complete relief. And when, as here, the public interest is vitally involved in the legality of fares charged by a public utility, not only are the inherent equity powers of the District Court available for the proper and complete exercise of that jurisdiction, but those equitable powers assume an even broader and more flexible character than when only a private controversy is at stake. Indeed, the court may go beyond the matters immediately underlying its equitable jurisdiction and give whatever other relief may be necessary in the circumstances. Mitchell v. Robert De Mario Jewelry, Inc., 361 US 288 (1960); U.S. v. Morgan, 307 U.S. 183 (1939); Virginian Ry Co. v. Federation, 300 U.S. 515 (1937). There is no need for remand to the Commission to provide for an appropriate order of restitution creating a fund for the benefit of transit riders as a class. Washington Gas Light Company v. Baker, 90 U.S. App. D.C. 98, 104-105; 195 F2d 29, 35 (1951).



While the District Court should be directed to order Transit to establish a fund in an amount equal to the unlawful fares collected, we realize that it may be inequitable to order Transit to segregate an amount of cash fully equal to the amount of the unlawful fares. A considerable portion of these monies may have been paid out in dividends or reinvested in equipment. We therefore suggest that the District Court, in framing an order of restitution in the exercise of its discretion as a court of equity, be authorized to provide that in lieu of segregating cash, this fund be established, in whole or part, by means of a special account or reserve on the books of the Company, and that the Court also be authorized to provide that appropriate offsetting adjustments be made in other accounts of the Company. In formulating its order of restitution the District Court should consider the recommendations of all interested persons, including the parties to this suit and the Washington Metropolitan Area Transit Commission. The utilization and disposition of this transit riders' fund should be left to the discretion of the authority with rate-making power over Transit in the future, consistent with the purposes for which this Court orders the fund established.



IV

PAYMENT OF FEES AND EXPENSES

As appellants have acted to establish a fund for the benefit of the transit-riding public as a class, Transit should be directed to pay reasonable attorneys' fees to counsel for appellants, including appellants for their services as counsel pro se, before the Commission and courts, reasonable fees for expert witnesses and reimbursement of expenses of litigation not included within taxable costs. Such payments should be charged to the fund ordered to be established for the benefit of transit riders by the judgment of this Court. Washington Gas Light Company v. Baker, 90 U.S. App. D.C. 98; 195 F2d 29 (1951).

Respectfully submitted,

/s/ Harold Leventhal

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Harold Leventhal

/s/ Leonard N. Bebhick

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Leonard N. Bebhick

/s/ Leonard S. Goodman

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Leonard S. Goodman

Counsel for Appellants

February 11, 1963

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

---

Leonard N. Bebhick, et al.,

Appellants,

v.

Public Utilities Commission of  
the District of Columbia, et al.,

Appellees.

---

No. 16,454

ORDER OF JUDGMENT

This case having come on for hearing by the Court en banc and the Court having issued its opinion of January 31, 1963, finding that the Order of appellee Public Utilities Commission, here challenged, which authorized and directed appellee D. C. Transit System, Inc. to charge a 25-cents cash fare for transportation of passengers within the District of Columbia was unlawful and must be set aside, and upon consideration of memoranda submitted by the parties as to the appropriate form of judgment, the Court hereby enters judgment as follows:

(1) There is hereby reversed, set aside, vacated and annulled --

(a) Order No. 4631 of the appellee Public Utilities Commission, dated March 2, 1960, authorizing and directing an increase of 5 cents in the cash fare from 20 cents to 25 cents charged by appellee D. C. Transit System, Inc. for the transportation of passengers within the District of Columbia.

(b) The Order of the District Court, dated June 5, 1961, in Civil Action 1529-60, affirming Order No. 4631 of appellee Public Utilities Commission.

(2) Appellee D. C. Transit System, Inc. is hereby ordered to amend and supplement any and all tariff filings which became effective on or after March 6, 1960, and which set forth a cash fare of 25 cents, so as to cancel the said 5-cent increase and reinstate a 20-cent cash fare for transportation of passengers within the District of Columbia, said amendments and supplements to be effective, nunc pro tunc, as of the date on which said tariff filings became effective.

(3) The proceeding is hereby remanded to the District Court with directions to enter orders in the exercise of its equity jurisdiction as follows:

(a) Directing D. C. Transit System, Inc. to segregate and establish a fund equal to twenty percent (20%) (5/25) of the cash fares collected by the Company for transportation of passengers within the District of Columbia from and after March 6, 1960, to the effective date of the tariff cancellations and amendments provided for in paragraph #2;

Further Ordering that such fund shall be used for the benefit of transit riders in future rate proceedings, including specifically but not exclusively for the purpose of absorbing cost increases which would otherwise require fare increases and enabling the institution of fare reductions;

Provided However, that the District Court in the exercise of its equitable discretion and upon consideration of the recommendations of interested persons, including the parties hereto and the Washington Metropolitan Area Transit Commission, may provide that in lieu of segregating cash, such fund be established, in whole or part, by means of a special account or reserve on the books of the D. C. Transit System, Inc.;

Further Provided, that the District Court, if it deems it appropriate in its discretion as a court of equity, may provide that the establishment of such fund may be accompanied, in whole or part, by appropriate offsetting adjustments in the other accounts of D. C. Transit System, Inc.

(b) Directing D. C. Transit System, Inc. to pay appellants' expenses of litigation not included within taxable costs, reasonable attorneys' fees to counsel for appellants, including appellants for their activities as counsel pro se before the Commission and the courts, and reasonable fees for expert witnesses, as may be determined by the District Court, taking into account the benefit to transit riders resulting from these services, such payments to be charged to the fund established pursuant to paragraph 3(a).

(4) Appellee D. C. Transit System, Inc. is ordered to pay taxable costs of appellants pursuant to Rule 20(c).

UNITED STATES COURT OF APPEALS  
For the District of Columbia Circuit

\_\_\_\_\_  
No. 16,454  
\_\_\_\_\_

United States Court of Appeals  
for the District of Columbia Circuit

FILED FEB 11 1963

LEONARD N. BEBCHICK, et al.,

*Nathan J. Paulson*  
CLERK  
APPELLANTS

v.

PUBLIC UTILITIES COMMISSION  
FOR THE DISTRICT OF COLUMBIA, et al.,

APPELLEES

\_\_\_\_\_  
MEMORANDUM SUBMITTING VIEWS OF APPELLEE PUBLIC  
UTILITIES COMMISSION AS TO FORM OF JUDGMENT  
APPROPRIATE TO CARRY OUT COURT'S OPINION

I

The order of the District Court dated June 5, 1961 (C.A. 1529-60) affirming Order No. 4631 of appellee Commission is hereby reversed.

II

The District Court is hereby ordered to vacate the aforesaid Order No. 4631 and remand the case to the Public Utilities Commission for such consideration and action as may be required to conform with the opinion and the judgment entered in this case.



### **III**

Upon remand the Commission shall:

1. Reconsider the accruals allowed for the estimated costs of track removal and repaving including a thorough inquiry into the economies contemplated by the Franchise Act and the extent to which economies due to recapping tracks instead of removing them would affect the estimated cost of track removal and repaving.

2. Adjust allowance for depreciation so as to eliminate depreciation on transit buses with a service life exceeding 14 years.

3. Reconsider the depreciation allowance on abandoned rail property to determine and make a finding upon whether Transit's investors have in the past been compensated for assuming the risk that the property would have to be abandoned before the investment in the property was entirely recovered.

4. If upon reconsideration of the foregoing items, the Commission determines that all or a portion of the cash fare increase for the period March 6, 1960 to January 18, 1961 was not justified, the Commission shall include in its order a requirement for the appropriate accounting thereof.

#### **JURISDICTIONAL MATTER**

Appellee Commission is fully aware of the fact that ultimate determination of track removal and repaving costs and provisions therefor,

and disposition of any special accounts to be established by virtue of this Court's judgment must be made by the Commission (Washington Metropolitan Area Transit Commission) now having regulatory jurisdiction over Transit. Therefore, for practical purposes it is suggested that the Court may wish to incorporate in its judgment a statement to the effect that its judgment is without prejudice to the right of the Washington Metropolitan Area Transit Commission, to exercise any powers which it may have under Title II, Sec. 23 (b) of the Compact (Public Law 86-794, 74 Stat 1031) once the matter is remanded to the Commission.

Respectfully submitted,

CHESTER H. GRAY  
General Counsel

GEORGE F. DONNELLA  
Counsel

ANDREW G. CONLYN  
Counsel

Attorneys for Appellee Public  
Utilities Commission  
District Building  
Washington 4, D. C.

#### CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Memorandum was mailed, postage prepaid, this 11<sup>th</sup> day of February, 1963, to Harold Leventhal, Esq., 1632 K Street, N. W., Washington 6, D. C., attorney

for appellants, and to Harvey M. Spear, counsel for appellee Transit,  
3600 M Street, N. W., Washington, D. C.

**GEORGE F. DONNELLA**  
Counsel

UNITED STATES COURT OF APPEALS  
FOR THE DISTRICT OF COLUMBIA CIRCUIT

United States Court of Appeals  
for the District of Columbia Circuit

No. 16454

FILED FEB 11 1963

LEONARD N. BEBCHICK, ET AL., APPELLANTS

*Nathan J. Paulson*  
CLERK

v.

PUBLIC UTILITIES COMMISSION, ET AL., APPELLEES

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MEMORANDUM OF APPELLEE, D. C. TRANSIT SYSTEM, INC.,  
AS TO THE FORM OF JUDGMENT APPROPRIATE TO CARRY OUT  
THE COURT'S OPINION DATED JANUARY 31, 1963

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I.

RECOMMENDED FORM OF JUDGMENT

In accordance with the Opinion of the Court dated January 31, 1963, appellee D. C. Transit System, Inc. respectfully submits the following Recommended Form of Judgment to carry out the Court's Opinion:

The judgment of the District Court entered June 5, 1961, is reversed and Order No. 4631 of the Public Utilities Commission entered March 2, 1960, is vacated. This case is remanded to the District Court with directions to remand the case to the Washington Metropolitan Area Transit Commission for further hearings; for such further findings of

fact and conclusions of law; and for such order as may be necessary and proper in the light of the Court's Opinion dated January 31, 1963.

II.

NO OTHER FORM OF JUDGMENT  
WOULD BE APPROPRIATE

In order to implement the Opinion of the Court dated January 31, 1963, extensive review procedures and findings of fact must be made by the administrative agency having primary responsibility for transit rate regulation in this area. The Court's Opinion can only be effectuated after such detailed findings of fact and rate-making determinations have been made. Such determinations and findings would be wholly beyond the jurisdiction of this Court and we respectfully submit should not be assumed by it.

As the Court pointed out in its Opinion, the jurisdiction of the Court on this appeal was limited by the provisions of Section 43-706 of the District of Columbia Code which provides as follows:

In the determination of any appeal from an order or decision of the Commission the review by the Court shall be limited to questions of law, including constitutional questions; and the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary, or capricious.

It is essential that all basic findings of fact be made by the appropriate regulatory agency and that the Court not be placed in the position of substituting its judgment for that of such agency. This the Court recognized when it stated in its Opinion:

We come to our conclusion not without awareness that we are not the regulatory body having primary responsibility for utility rate regulation in this jurisdiction.

Any judgment substantially different from the one suggested above would necessarily involve this Court in a determination of purely factual questions. Such factual questions would include not only the numerous questions presented by the Court's conclusions as to (1) track removal and repaving charges, (2) depreciation charges for buses, and (3) depreciation charges for abandoned rail properties, but they would also include the basic regulatory inquiries as to what the proper rate of return should have been during the period in question (March 2, 1960 to January 18, 1961).

The Court has recognized that such questions should in the first instance, be resolved by the regulatory agency. In its Opinion herein, the Court quoted with approval the following language from its opinion in



Washington Gas Light Co. v. Baker, 88 U.S. App. D.C. 115,  
123, 188 F.2d 11, 19 (1950), Cert. denied 340 U.S. 952  
(1951):

It is not for us to say \* \* \*  
whether or not the risk of obsolescence  
\* \* \* was borne by the investor in the  
past and whether he was compensated for  
it. That is an inquiry which must be  
made in the first instance by the Com-  
mission.

It is obvious, therefore, in order to carry out  
the Opinion of the Court that there must be a remand to  
the regulatory commission for further hearings; for further  
findings of fact and conclusions of law; and for such order  
as may be necessary in light of this Court's Opinion of  
January 31, 1963.

### III.

THE CASE SHOULD BE REMANDED TO  
THE WASHINGTON METROPOLITAN  
AREA TRANSIT COMMISSION

A question may be raised as to the proper commis-  
sion to which the remand should be directed. We submit  
that for the reasons hereinafter set forth the remand can  
only be to the Washington Metropolitan Area Transit  
Commission which now has sole and exclusive jurisdiction

over the fares, regulations and practices of this appellee.

Although the Commission which entered the order vacated herein was the Public Utilities Commission of the District of Columbia, the jurisdiction of that Commission over this appellee terminated on March 22, 1961, pursuant to the Joint Resolution of the Congress dated September 15, 1960, Public Law 86-794, 86th Congress, 74 Stat. 1031.

Since March 22, 1961, exclusive jurisdiction over all matters affecting the fares, regulations and practices of this appellee has been vested in the Washington Metropolitan Area Transit Commission, which was created for the express purpose of taking over the jurisdiction of several local regulatory agencies including the Public Utilities Commission of the District of Columbia.

Section 3 of the Consent Legislation of Public Law 86-794, 74 Stat. 1031 at 1050, provides as follows:

That, upon the effective date of the compact [March 22, 1961] and so long thereafter as the compact remains effective, the applicability of the laws of the United States, and the rules, regulations, and orders promulgated thereunder, relating to or affecting transportation under the compact and to the persons engaged therein, \* \* \* relating to the powers of the Public Utilities Commission of the District of Columbia \* \* \*, is suspended \* \* \*.

Paragraph 23(b) of Title II of Public Law 86-794 further provides as follows:

To the extent that the Commission [Washington Metropolitan Area Transit Commission] determines such action to be necessary or appropriate in the exercise of the powers and duties vested in or imposed upon it by this Act, such Commission shall continue and carry to a conclusion any proceedings, hearings, or investigation which, at the time this compact takes effect, is pending before the Public Utilities Commission of the District of Columbia, \* \* \*. In the event the Commission assumes jurisdiction in any such case, it shall be governed by the provisions of this compact and not by the provisions of law applicable at the time the proceedings were instituted.

See also Title I, Article VIII; Title II, Article XII, paragraphs 20(a), and 21 of Public Law 86-794.

All of the questions posed by the Court's Opinion are now under consideration by the Washington Metropolitan Area Transit Commission, although for a different period of time.

As pointed out in the Dissenting Opinion of Judges Burger and Miller, the "entire matter of transit rates" is now under review by the Washington Metropolitan Area Transit Commission in a new rate proceeding involving the schedule of fares of appellee D. C. Transit System, Inc.

The members of the Washington Metropolitan Area Transit Commission are fully cognizant of all phases of the operations of appellee D. C. Transit System, Inc. as they have been conducted in the past and are currently being

conducted. The members of the Public Utilities Commission, however, are unfamiliar with the affairs of appellee D. C. Transit System, Inc. inasmuch as the entire membership of that Commission has changed since Order No. 4631 was entered on March 2, 1960. Since March 22, 1961, the effective date of Public Law 86-794, the Public Utilities Commission has neither claimed nor exercised any jurisdiction over the fares, regulations and practices of appellee D. C. Transit System, Inc.

Since the Washington Metropolitan Area Transit Commission is currently working on determinations involving all of the same issues as were raised in this Court's Opinion, it is in the best interest of all parties concerned to avoid the duplication and confusion which would result if the same issues were to be subjected to review for prior periods by another agency, particularly where the other agency has no current jurisdiction or control over any of the fares, regulations or practices of appellee D. C. Transit System, Inc.

Appellee D. C. Transit System, Inc. is not alone in its conclusion that this case should be remanded to the Washington Metropolitan Area Transit Commission. In their

Brief herein (Page 71, footnote 29)\*/, the appellants also concluded that, in the event of remand, the case should be remanded to the Washington Metropolitan Area Transit Commission.

Respectfully submitted,

/s/ Harvey M. Spear

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Harvey M. Spear  
3600 M Street, N. W.  
Washington 7, D. C.

/s/ John R. Sims, Jr.

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John R. Sims, Jr.  
3600 M Street, N. W.  
Washington 7, D. C.

Of Counsel:

Hogan & Hartson  
800 Colorado Building  
Washington 5, D. C.

Attorneys for Appellee  
D. C. Transit System, Inc.

By /s/ Edmund L. Jones  

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Edmund L. Jones

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\*/ The following is footnote 29 as it appears on Page 71 of appellant's Brief herein:

"Upon remand to the Commission, the Washington Metropolitan [Area] Transit Commission may, in its discretion, take over the final disposition of this proceeding. See Compact, Title II, Section 23."

CERTIFICATE OF SERVICE

Copies of the foregoing Memorandum were mailed, postage prepaid, to Leonard N. Bebhick, Esquire, 1 Farragut Square South, N. W., Washington, D. C., Leonard S. Goodman, Esquire, 4337 River Road, N. W., Washington, D. C., George F. Donnella, Esquire, District Building, Washington, D. C., and Harold Leventhal, Esquire, 1632 K Street, N. W., Washington, D. C., this 11th day of February, 1963.

/s/ John R. Sims, Jr.

---

John R. Sims, Jr.



UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

United States Court of Appeals  
for the District of Columbia Circuit

Leonard N. Bebchick, et al.

Appellants

v.

Public Utilities Commission of  
the District of Columbia, et al.

Appellees

FILED FEB 25 1963

No. *Nathan J. Paulson*  
CLERK

PETITION FOR ANCILLARY RELIEF

Appellants hereby move this Court to provide ancillary relief by staying Commission Order No. 4735, dated January 18, 1961, insofar as it authorizes and directs Transit to collect a 25 cent cash fare for transporting passengers in the District of Columbia.<sup>1/</sup> This stay is requested pending a judicial determination of an appeal challenging the validity of Order No. 4735 now pending in the District Court (C.A. No. 825-61).

1. This action is necessary to make effective the Court's review jurisdiction and to preserve for Transit riders the fruits of the judgment entered on February 21, 1963.

Such a stay procedure is needed to enable a judgment of this Court setting aside a Commission order to become effective notwithstanding the issuance during the course of litigation of

<sup>1/</sup> The Court may require Transit to amend its tariffs so as to cancel the 25 cent cash fare and to reinstate a 20 cent cash fare. The Commission may be enjoined from enforcing Order No. 4735 to the extent it directs Transit to charge a 25 cent cash fare.

a subsequent Commission order continuing in effect the order under appeal authorizing a 25 cent cash fare.

2. In issuing Order No. 4735 which continued in effect the 25 cent cash fare, the Commission rejected an increase in Transit's token fare which the Company had requested only six months after Order No. 4631 itself had issued. Insofar as the Commission in Order No. 4735 rejected the intervenors request for reinstatement of the 20 cent cash fare it merely repeated the rulings underlying Order No. 4631 which this Court has found to be unlawful. This appears on the face of Order No. 4735 and the supporting Opinion (38 PUR 3d 19):

(a) The Commission refused to reduce the annual provision for track removal and repaving, of \$1,044,196 per annum, stating "it is the opinion of the Commission that the present program of amortization should not be abandoned" (p. 44). The Commission referred to its previously indicated intention of continued scrutiny, although the record established that Transit had on hand an unexpended reserve for track removal and repaving considerably in excess of its actual requirements through fiscal 1966. Moreover, the Commission reiterated as justification for the accrual Transit's theoretical liability under its Franchise to remove all the tracks and repave the track areas. The Commission also continued to assume incorrectly that Transit itself would have to bear the total cost of such a hypothetical program.

(b) Although the Commission agreed to change its methods for the future so as to eliminate further depreciation on fully depreciated buses, it continued such depreciation for half of the "test period." This error is thus part of the bases for Order No. 4735.

(c) The Commission continued to allow depreciation on abandoned rail properties without any inquiry or findings regarding whether the risk of obsolescence was borne by Transit's investors in the past and whether they had been compensated for it. Washington Gas Light Co. v. Baker, 88 U.S. App. D.C. 115, 188 F2d 11 (1950), cert. denied, 340 U.S. 952 (1951).

3. It may be that the judgment formally setting aside Order No. 4735, insofar as it continues the 25 cent cash fare, should be entered in the judicial proceeding wherein that Order is under appeal. However, this Court should enter the stay requested in furtherance of its undeniable jurisdiction under 28 U.S.C. §1651 (All Writs Statute) and the well settled Federal judicial power to provide ancillary relief to secure or preserve the fruits and advantages of a judgment or decree already rendered -- a power which extends to providing injunctive relief in an ancillary proceeding even where outside the jurisdiction of the court in an original proceeding, Local Loan Co. v. Hunt, 292 U.S. 234, 239 (1934). The inherent power of this Court is underscored by Scripps-Howard Radio v. F.C.C., 316 U.S. 4, 9 (1942); cf. Public Utilities Comm. v. Capital Transit Co., 94 U.S. App. D.C. 140, 214 F2d 242, 245 (1954).

4. The present cause is an appropriate one for this Court to exercise its discretion to grant the stay:

(a) The stay is needed to protect Transit riders from immediate and irreparable injury. Transit collects an average of 2-1/2 million cash fares a month. Where overpayments are already collected, all that a court can do is establish a fund for the benefit of future riders. This falls short of providing full restitution to individual riders who have paid an unlawful fare.

(b) There is a patent satisfaction of the requirement that applicants make a showing of the likelihood of success -- likelihood that Order No. 4735 will be set aside on the merits. To argue otherwise would be spurious.

(c) Granting appellants ancillary relief would cause Transit no possible prejudice or injury. Transit may intone the theoretical contingency that Order No. 4735 may somehow be preserved notwithstanding the Court's action in setting aside Order No. 4631. But the Court can readily protect Transit by providing that in such event Transit regain the revenues that otherwise would have been earned during the period of stay by making an appropriate withdrawal or charge against the Transit riders' fund provided by the Court's judgment of February 21, 1963.

(d) It is anticipated that Transit may apply to continue the 25 cent cash fare and offer to fund the 5 cent amounts involved and issue receipts to each cash fare rider

redeemable on final judgment. These would be minimal conditions for maintaining a 25 cent cash fare. Yet even they do not avoid irreparable injury to transients and visitors to Washington who ride the buses. This course should be considered only if Transit intends to petition the Supreme Court for a writ of certiorari and this Court then determines to stay its judgment and relief ancillary thereto.

5. Finally, it is suggested that this Court make appropriate provision for the expeditious presentation and determination of the appeal from Order No. 4735 in a manner consistent with its Opinions and Judgment. This Court may further suggest to the District Court the propriety of invoking Title 43, Section 708 of the District of Columbia Code and certifying to this Court the question whether the appeal from Order No. 4735 is governed by this Court's Opinion and Judgment setting aside Order No. 4631.

WHEREFORE, appellants pray that an appropriate order of ancillary relief be entered in the premises.

Respectfully submitted,

/s/ Harold Leventhal  
Harold Leventhal

/s/ Leonard N. Bebchick  
Leonard N. Bebchick

/s/ Leonard S. Goodman  
Leonard S. Goodman

Counsel for appellants

February 25, 1963

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing Petition for Ancillary Relief was served personally upon Harvey Spear, counsel for appellee Transit, by leaving a copy with the person in charge of his office, D. C. Transit System, Inc., 3600 M Street, N. W., Washington, D. C., and upon George F. Donnella, counsel for appellee Commission, by leaving a copy with the person in charge of his office, District Building, N. W., Washington, D. C., this 25th day of February, 1963.

/s/ Leonard N. Bebchick

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Leonard N. Bebchick



UNITED STATES COURT OF APPEALS  
FOR THE DISTRICT OF COLUMBIA CIRCUIT

United States Court of Appeals  
for the District of Columbia Circuit

FILED MAR 2 1963

*Nathan J. Paulson*  
CLERK

LEONARD N. BEBCHICK, et al.,  
Appellants,

v.

No. 16,454

PUBLIC UTILITIES COMMISSION OF  
THE DISTRICT OF COLUMBIA, et al.,  
Appellees.

OBJECTION OF D. C. TRANSIT SYSTEM, INC.  
TO APPELLANTS' PETITION FOR ANCILLARY RELIEF

The petition of the appellants is beyond the jurisdiction of this Court, presents matters not in any record before this Court and should be denied.

I. This Court Lacks Jurisdiction to Enter The  
Relief Requested By Appellants.

Appellants request this Court temporarily, at least, to revoke an outstanding order of the Public Utilities Commission of the District of Columbia which became effective on January 18, 1961. Thus, the appellants are not requesting a stay, but affirmative relief against an order that is presently under review by the United States District Court for the District of Columbia.

An orderly process for appeals from orders of the Public Utilities Commission is prescribed by statute. 43 D.C. Code (1961 Ed.) §705. This statute provides that an order of the Commission may be first appealed to the United States District Court for the District of Columbia, then to this Court and, thereafter, a petition for certiorari

may be filed in the Supreme Court of the United States. No authority is given this Court to take jurisdiction of such a case until after the District Court has entered its order or decree.

The applicable statutory provision governing a stay of an order of the Commission, as set forth in 43 D.C. Code (1961 Ed.) §707, provides:

All orders and decisions of the Commission shall remain in full effect, except as provided in section 43-704 hereof, unless and until they are suspended, superseded, or rescinded by the Commission or are vacated by lawful order of the District Court of the United States for the District of Columbia: Provided, That if in any petition made to the said court appealing from an order or decision of the Commission it be alleged that substantial and irreparable property loss would be occasioned to the petitioner by the operation of the said order pending the determination of the said appeal, the court shall set a time and place for hearing upon the said allegation after not less than three days' notice to the Commission (during which period the execution of the order or decision shall be stayed), and the said court may then, upon a clear showing of the irreparable and substantial property loss as alleged, suspend the effective date of the said order. No such suspension shall be for a greater period than sixty days without further order after notice or hearing by the court. In the event of the issuance of an order suspending the operation of any order of the Commission, the court may include therein such provision as it deems advisable for the preservation of records or accounts and the impounding or otherwise securing of moneys necessary to give effect to the order of the Commission in the event the said order is sustained.

No application was made under this section for a stay in the District Court and the petition of appellants in that court did not allege "substantial and irreparable property loss" as required by the aforesaid section in order to permit a stay by the District Court. Furthermore, no hearing has been had as is required. Thus, inasmuch

as the District Court would have no authority to grant a stay,  
it is submitted that this Court does not possess such authority.

Without any effort to comply with the applicable statutory provisions, the appellants have bypassed the District Court and ask this Court not to stay the effective date of the Commission order but rather to revoke it and fix a rate different from that provided therein. Appellants assert that this Court should either require Transit to amend its tariffs so as to cancel the 25¢ cash fare and reinstate a 20¢ cash fare, or that the Commission be enjoined from enforcing Order No. 4735. (Appellants' Petition, p. 1, n. 1). Such relief would clearly be mandatory in nature and would be premature inasmuch as the Commission order is not before this Court.<sup>1/</sup> Consequently, it is beyond the jurisdiction of this Court to grant the requested relief.<sup>2/</sup>

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<sup>1/</sup> North Carolina Natural Gas Corp. v. United States, 200 F. Supp. 745, 751-53 (D. Del. 1961) (Three Judge District Court.)

<sup>2/</sup> The jurisdiction of this Court over an order of the Commission is limited to an appeal from an order or decree of the District Court. 43 D.C. Code (1961 Ed.) §705. No such court order or decree is before this Court and, therefore, it is without power to act. To paraphrase the words of the Third Circuit under a different statutory review provision, the mere fact that review is provided for by a Court of Appeals after appropriate proceedings have been completed below neither authorizes nor in any way suggests judicial intervention at an earlier stage than that provided for by the statute. Greater Delaware Valley Fed. Sav. & Loan Ass'n v. Federal Home Loan Bank Board, 262 F.2d 371, 373 (3rd Cir. 1958).

Further the relief requested would involve this Court in the administrative process of rate making.<sup>3/</sup> This Court, even when an appeal is before it, is not "entitled to revise the Commission's decision and to enter such judgment as the Court may think just." It is not empowered "to make an administrative judgment." Compare Federal Radio Com'n. v. Nelson Bros. Bond & Mortgage Co., 289 U.S. 266, 276-77 (1933), with Federal Radio Com'n. v. General Electric Co., 281 U.S. 464 (1930); see also, FCC v. Pottsville Broadcasting Co., 309 U.S. 134 (1940). As the Supreme Court said in United States v. Jones, 336 U.S. 641, 651-52 (1949):

The Railway Mail Pay Act gives the Interstate Commerce Commission exclusive jurisdiction to determine "fair and reasonable rates." The Urgent Deficiencies Act provided for judicial review of the Commission's rate orders in "cases brought to enjoin, set aside, annul or suspend such order." No power was given the reviewing court to revise them

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<sup>3/</sup> This Court in exercising its jurisdiction to review Commission orders, even when they are before it on appeal, is "limited to questions of law." 43 D.C. Code (1961 Ed.) §706. Under similar statutory review provisions it has been held by the Supreme Court that under no circumstances "can judicial action supplant the discretionary authority of the Commission. A federal court cannot fix rates . . . ." FPC v. Pacific Power & Light Co., 307 U.S. 156, 160 (1939). Or as stated in FPC v. Idaho Power Co., 344 U.S. 17, 20 (1952), "[T]he guiding principle, violated here, is that the function of the reviewing court ends when an error of law is laid bare. At that point the matter under review goes to the Commission for reconsideration."

when found invalid, or to render judgment for any amount ~~thought~~ to be due under such a revision. (Emphasis added.) 2/

The statutory authority cited by the appellants is not applicable to this proceeding. This Court, like other federal courts, under 28 U.S.C.A. §1651 admittedly may in a separate proceeding "issue all writs necessary or appropriate in aid of their jurisdictions and agreeable to the usages and principles of law." The so-called stay requested by appellants would not be in aid of this Court's appellate jurisdiction, for when the District Court acts, then this Court on timely appeal may exercise its review function under 43 D.C. Code (1961 Ed.) §705. There is no threat to this Court's jurisdiction, and what appellants seek is in reality an attempt to bypass the District Court. Likewise, as pointed out in the previously cited cases, any action by this Court along the lines requested by appellants would not be "agreeable to the usages and principles of law" but would be

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4/ To the same effect is United States v. Public Utilities Commission, 81 U.S. App. D.C. 237, 241 n. 9, 158 F.2d 533, 537 n. 9 (1946), in which the United States argued that a certain amount should have been trimmed from the rate base, and the Court said:

We note in the argument before this court counsel for the Government did not specify how much of the \$29,000,000 surplus should be trimmed from the rate base. Hence, if we were to hold that it was not an appropriate element, it would become our duty to specify, in dollars and cents, the amount to be taken out. This, we think, would be the clearest sort of usurpation of the Commission's authority. (Emphasis supplied.)

contrary thereto. The "all writs" section "may not appropriately be used merely as a substitute for the appeal procedure prescribed by the statute." Roche v. Evaporated Milk Ass'n., 319 U.S. 21, 26 (1943). Nor may it be resorted to because of the delay and inconvenience attendant to a District Court trial before an appeal will lie to the Court of Appeals. Id. at 30. It is likewise clear that 28 U.S.C.A. §1651 does not give to a court of appeals "a general roving commission to supervise the administration of justice in the federal district courts" within their circuits. See, e.g., In re Sylvania Electric Products, 220 F.2d 423, 424 (1st Cir. 1955). Furthermore, the relationship between federal courts and administrative agencies is not that of federal courts inter se and, therefore, the "all writs" statute is inapplicable. FCC v. Pottsville Broadcasting Co., 309 U.S. 134, 141 (1940); Scripps-Howard Radio, Inc. v. FCC, 316 U.S. 4, 21 (1942) (dissent).

Neither Scripps-Howard Radio, Inc. v. FCC, 316 U.S. 4 (1942), nor Public Utilities Commission v. Capital Transit Company, 94 U.S. App. D.C. 140, 214 F.2d 242 (1954), supports the appellants' petition that this Court has jurisdiction to enter a stay of a Commission order that is not before it, for in both cases the court entering the stay had valid jurisdiction on appeal of the order under the applicable statute.

The doctrine of ancillary jurisdiction is completely inapposite to the petition of appellants. This Court in this proceeding has



entered its judgment on Commission Order No. 4631. Commission Order No. 4735 is not before this Court but rather before the District Court under the applicable statutory review procedure provided by Congress. Nothing transpiring in the District Court proceeding involving Order No. 4735 can in any way affect this Court's judgment involving Order No. 4631, and, therefore, there is no necessity for any ancillary relief.<sup>5/</sup>

II. Appellants Have Failed To Meet The Heavy Burden Required To Obtain A Stay Of An Administrative Order

In order to obtain a stay of an administrative order, even when it is before the Court on appeal, a party must demonstrate that he is likely to prevail on the merits and that irreparable injury is likely to occur if a stay is not granted. Air Line Pilots Ass'n. v. C.A.B., 215 F.2d 122, 125 (2d Cir. 1954) (J. Harlan). Thus, it has been established that a stay of an administrative order will only be granted when the movant satisfies the following conditions: (1) a substantial likelihood of success on the merits; (2) irreparable injury to the petitioner; (3) no substantial harm to other interested persons.

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<sup>5/</sup> In this Court's opinion of February 21, 1963 it is stated that "Transit continues to charge the 25 cent cash fare under Commission Order No. 4735" and suggests a motion to stay this order be filed. (Slip Opinion, pp. 2 & 3). It is necessary to point out that this is not correct. This appellee currently collects a 25 cent cash fare pursuant to a tariff filed with and accepted by the Washington Metropolitan Area Transit Commission under section 5 of the Washington Metropolitan Area Transit Regulation Compact. 74 Stat. 1031, 1 D.C. Code (1961 Ed.) §1410. Transit is required by law to charge the fare set forth in this tariff. Ibid. Thus, it is not Commission Order No. 4735, which appellants seek to stay, that establishes and requires a 25 cent cash fare.

and (4) no harm to the public interest. Eastern Air Lines v. C.A.B., 261 F.2d 830 (2d Cir. 1958); Virginia Petroleum Jobbers Ass'n. v. FPC, 104 U.S. App. D.C. 106, 110, 259 F.2d 921, 925 (1958).

The appellants have failed to satisfy any of these conditions. The record in regard to Commission Order No. 4735 is presently before the District Court. There is no way this Court can assess appellants' likelihood of prevailing on the merits. Furthermore, the records in regard to Commission Order No. 4735 and Commission Order No. 4631 are materially different. In the two proceedings different evidence and exhibits were introduced, different test years were involved and materially changed circumstances had occurred.<sup>6/</sup> Thus, it can be said that there is no substantial identity between the two records.

Appellants' contention of prevailing on the merits is also premised on the fact that the decision and judgment invalidating Order No. 4631 will be sustained.<sup>7/</sup> It is respectfully submitted that the judgment of February 21, 1963 is clearly an assumption of the administrative

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<sup>6/</sup> In Commission Order No. 4735 the Commission in shifting the method of bus depreciation assumed on the basis of incomplete study that Transit was overdepreciated. When a complete depreciation study was completed the Commission found that in fact Transit was underdepreciated. See Commission Order No. 4754, a copy of which is attached hereto.

<sup>7/</sup> This order was sustained by the District Court and by a panel of this Court (2-1) and then reversed by this Court en banc (5-4). Thus, of the 10 federal judges who have considered it, there has been an even division (5-5).

discretion reposed by Congress in the Public Utilities Commission and amounts to unauthorized rate making by this Court, which has been held by the Supreme Court on numerous occasions to be improper. Therefore, counsel for this appellee have been instructed to file a petition for certiorari in the Supreme Court to review this judgment.

In United States v. Jones, 335 U.S. 641, 670-71 (1949), the Court in condemning an attempt by a reviewing court to engage in rate making, after finding a Commission order invalid, said:

This not only would short-circuit the Commission in the rate-making process, but would involve substituting the court's judgment for the Commission's as to the amount of any new rate which might be fixed.

If the relief requested by appellants is granted and the cash fare rolled back to 20¢, it would result in a loss to Transit of approximately \$4,100 a day, which could never be recovered. This loss would certainly "substantially harm" Transit and would not be in the public interest for it would seriously jeopardize Transit's ability to provide adequate service and in fact would raise a serious question as to its ability to remain in business.

### III. Conclusion

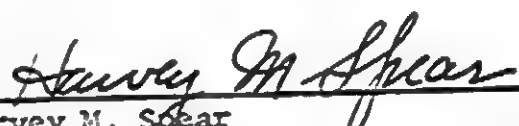
The relief requested by the appellants is beyond this Court's jurisdiction as the order in question is presently before the District Court under the applicable statutory review procedure prescribed by Congress. Any summary order by this Court would violate the intent of Congress and would be contrary to the specific statutory provision requiring a hearing and finding of "irreparable and substantial property loss" 43 D.C. Code (1961 Ed.) §707.


The result of granting the appellants relief would be an actual cash loss to Transit of \$4,100 a day, which could never be recovered and which "would have a serious adverse effect on" its ability to provide adequate service. This factor alone should preclude the granting of a stay.

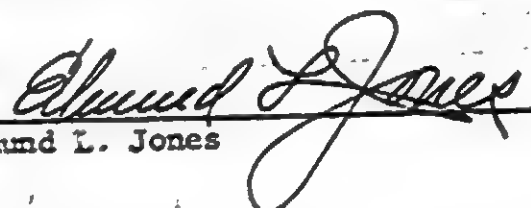
Finally, as heretofore stated the present fare is being charged pursuant to a tariff filed with the Washington Metropolitan Area Transit Commission and this appellee is required by law to charge the rates prescribed therein.


For the reasons set forth herein it is clear that appellants' petition is entirely without merit, is factually incorrect and not supported by statutory or decisional law and, therefore, should be denied.

Respectfully submitted,

  
Harvey M. Spear

  
John R. Sims, Jr.  
3600 M Street, N.W.  
Washington 7, D. C.

  
Edmund L. Jones

  
John J. Ross  
800 Colorado Building  
Washington 5, D. C.

Attorneys for Appellee,  
D. C. Transit System, Inc.

CERTIFICATE OF SERVICE

Copies of the foregoing Objection were mailed, postage prepaid, to Leonard N. Bebhick, Esquire, 1 Farragut Square South, N.W., Washington, D. C., counsel for appellants, and George F. Donnella, Esquire, District Building, Washington, D. C., counsel for the Public Utilities Commission, Washington, D. C., this 2nd day of March, 1963.

  
\_\_\_\_\_  
John J. Ross  
Attorney for Appellee

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

Order No. 4754

May 24, 1961

IN THE MATTER OF )  
 )  
A Study of the Depreciation Reserves, ) P. U. C. No. 2900/4  
Rates and Practices of D. C. TRANSIT )  
SYSTEM, INC. )

This Commission is required by law to establish proper and adequate rates of depreciation of the several classes of property of each public utility (Section 8, Par. 16, Public Law No. 435). In compliance with the statutory requirement, the Commission periodically reviews the prescribed depreciation rates, practices and accumulated reserves, and checks the application of the prescribed rates and the charges and credits to the depreciation reserve as part of the regular and continuing audit of each utility under its jurisdiction. From time to time it becomes necessary to make a special detailed study of the depreciation rates and practices of a utility. The need for such a particular study of the depreciation rates and practices of D. C. Transit System, Inc. became apparent and was brought out by testimony in Formal Case No. 471, which ended February 19, 1960 and resulted in Order No. 4631, dated March 2, 1960 (see Page 16 of "Opinion in Support of Findings, Conclusions, and Order Promulgated March 2, 1960").

Subsequent thereto on June 16, 1960, the Commission employed Mr. John L. Ingoldsby, a registered professional engineer now retired from the staff of the Commission and engaged in consulting work, to:

- "(a) Review the existing depreciation rates of the Company to determine if any changes should be made to give effect to changed conditions since July 1, 1953, at which time the present rates were prescribed.
- (b) Study the adequacy or inadequacy of the reserve for depreciation presently recorded on the books.
- (c) Study the need, if any, for providing for extraordinary property losses related to rail facilities yet to be abandoned.



- (d) Determine the desirability of adopting the unit method of depreciating buses.
- (e) Report the results of the studies."

The study was completed and a report thereon submitted to the Commission on April 10, 1961. The Commission has carefully considered the report and is of the opinion that it is a comprehensive analysis of the subject matter.

While the study was in progress D. C. Transit filed for an increase in transit rates. During the course of the hearings on this transit rate matter, the part of the depreciation study relating to the investment in buses was completed, and Mr. Ingoldsby testified thereto and submitted exhibits reflecting the average service life of all the buses owned and operated by D. C. Transit System, Inc. and its predecessors.

The investment at June 30, 1960 in buses and accessory equipment amounted to \$20,425,176, which was by far the largest account among the plant accounts, and a primary reason why it was studied first.

The result of the study of the passenger bus portions of the depreciable property, which study was based upon the actual experience of the D. C. Transit System, Inc. and its predecessor companies, together with judgment as to future expectations, indicated that the fair and adequate components for use in the development of the depreciation rate appeared to be an average service life of 17.0 years, and an average net salvage of 2.5%. These factors produce a 5.74% rate for annual depreciation accruals. ( $100\% - 2.5\% \div 17 \text{ years} = 5.74\%$ ) It was these factors and this rate that Mr. Ingoldsby recommended to the Commission.

The report also contained a recommendation that a change be made from the existing "group" basis to a "unit" basis for the accrual of amounts for depreciation on buses. In the use of the group basis, the amounts of the monthly accruals were determined by the application of the depreciation rate to the total investment cost in Account 522 - Passenger Buses. This arrangement tended to permit accruals on some buses to exceed the investment cost. The unit basis, as used in the depreciation study, consists of a unit containing like items purchased at the same time rather than an individual bus. This unit basis will keep accruals from exceeding the investment cost.

Based upon Mr. Ingoldsby's recommendations that a service life of 17 years and 2.5% net salvage be adopted as the basis for an annual rate of depreciation applicable to buses, and that the unit method of depreciation also be adopted for buses, the Chief Accountant of the Commission adjusted the income statement for the twelve months ending February 28, 1961 to reflect such changes, and testified that in his opinion no other adjustments of depreciation rates were necessary at that time. The Commission considered the testimony and found that the adjustment of the bus depreciation rate and the adoption of the unit method was justified.

The complete Ingoldsby study now at hand fully supports the findings of the Commission in Formal Case No. 474. In summary, the Ingoldsby study finds that the estimated depreciation reserve requirement as of June 30, 1960 was \$27,287,231. In relation thereto, the actual depreciation reserve recorded on the books as of that date amounted to \$26,747,790. The indicated deficiency is only \$539,441, which will be eliminated if the Commission is sustained in requiring that certain proceeds from the sale of the Fourth Street Shop and Southern Carhouse be credited to the reserve for depreciation. The amount in litigation is \$613,661 and this amount will be added to the book depreciation reserve if the Commission is sustained.<sup>A</sup>

We agree with Mr. Ingoldsby that the total recorded reserve for depreciation is adequate and no adjustment to increase or decrease the reserve is indicated.

On Page 10 of the study Mr. Ingoldsby computes the amount of \$2,119,481 (Column 8) as the estimated annual accrual of depreciation expense based upon a 17-year life and 2.5% net salvage for buses, and upon various other rates of depreciation for the balance of the property. His computations do not include the amortization of the retirement loss of certain rail facilities abandoned as a result of conversion in January 1960. In the opinion of Mr. Ingoldsby the estimated annual depreciation accrual of \$2,119,481, based upon the investment in depreciable plant of \$45,485,785 as of June 30, 1960 will produce an adequate fund to properly provide for all future retirement losses, including a write-off of all rail facilities by August of 1963.

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<sup>A</sup>Since the completion of the Ingoldsby study, the United States Court of Appeals for the District of Columbia on May 18, 1961 issued its decision in the above matter (No. 15967, D. C. Transit System, Inc., Appellant v. Public Utilities Commission of the District of Columbia, Appellee) sustaining the finding of the District Court, which found the Commission's Order of September 30, 1959 was not unreasonable, arbitrary or capricious. The Court also found no constitutional question involved. The addition of \$613,661 to the reserve for depreciation will increase the recorded amount to \$27,361,451 as of June 30, 1960, which amount is \$74,220 greater than the requirement as computed by Mr. Ingoldsby.

In comparison therewith, the Chief Accountant of the Commission demonstrated via Exhibit No. 53, Formal Case No. 474, that the annual accrual for depreciation, using a 17-year life for buses and retaining the existing rates of depreciation for the balance of depreciable plant and continuing the special amortization of abandoned rail facilities as ordered in Formal Case No. 471, would amount to \$2,121,973, based upon an investment in depreciable plant as of July 31, 1960 in the amount of \$45,575,686.

Mr. Ingoldsby also recommends that the annual rate of depreciation applicable to limousines be reduced from 25% to 20%. This is the result of his determination that the service life of three years was proper but that the net salvage would be 40% instead of 25% as adopted by the Company. The effect of this adjustment would be to reduce the total annual accrual from \$2,121,973, as set forth above, to \$2,113,116. The difference of \$8,857 stems from the use of an annual depreciation charge applicable to limousines in the amount of \$35,447, as computed by Mr. Ingoldsby and shown on Page 12 of his report, instead of \$44,304 computed by the Company and adopted by the Chief Accountant in his Exhibit No. 53. In the opinion of the Commission an annual accrual of either \$2,121,973 or \$2,113,116 is near enough to the recommended accrual of \$2,119,481 to meet all the requirements of being proper and adequate. It must be remembered that the establishment of proper and adequate rates of depreciation is of necessity an estimate as the nature of the problem does not permit an exact and precise determination.

In view of the above, the Commission finds that the annual rate of depreciation applicable to limousines shall be 20% per annum, based upon a three-year life with net salvage at 40%. The Company will be directed to modify its charges for depreciation applicable to limousines in accordance with the above, effective February 28, 1961.

In consideration of the fact that a limousine, like a bus, is readily identifiable as a unit, the Commission also finds that the unit method of depreciation shall be utilized in computing depreciation on the investment in limousines. This will prevent excess accruals in the event that a limousine is retained in service longer than the estimated three years.

Since the annual rate of depreciation applicable to limousines is established at 20%, effective February 28, 1961, appropriate adjustment of the charges for depreciation applicable to the investment in limousines that have been recorded since that date must be made. As the estimated service life of limousines is three years, it is obvious that the annual rate of 20% is designed to accrue 60% of the investment via depreciation charges, with the remaining 40% stemming from the net salvage to be realized. Any limousine that has been depreciated prior to February 28,

1961 at the previous rate of 25% will have accumulated a greater amount of depreciation over the period from date of purchase to February 28, 1961 than would have been accumulated if the annual rate of 20% had been applied. This being so, the appropriate adjustment for such units requires the undepreciated portion of the loss in service value (60% of investment less depreciation accumulated to February 28, 1961) to be written off over the remaining estimated life. For example, if a limousine had been purchased two years prior to February 28, 1961, then 50% of the investment would have been accumulated to that date by the application of the annual rate of 25% for two years and the amount of depreciation to be written off in the year subsequent to February 28, 1961 must be 10% of the investment. The result would be to accumulate the indicated 60% of the investment over three years.

In the example above, if the new annual rate of 20% was applied during the year subsequent to February 28, 1961 the result would be to accumulate, in toto, 70% of the investment. This would constitute an excess accrual and would defeat the purpose of the adjustment in annual rate of depreciation. It should be clear that the service life is the controlling factor and the annual rate computed therefrom applies without modification only to investments that have not been partially depreciated at another annual rate at the time of change, February 28, 1961 in this case.

The Commission takes this opportunity to clarify its Order No. 4735 wherein under Section 7 the Company was directed to "----make appropriate adjustments on its books to reflect the changes in rate and method of depreciation applicable to buses, including spare parts and accessories, herein presented." It was contemplated that the remaining life method, as outlined above, would be the proper way to effect the "appropriate" adjustment, otherwise an excess amount of depreciation will be accumulated, or a unit will be fully depreciated in less time than the estimated service life (17 years for buses). To illustrate, consider a bus that had been purchased in August of 1953, one of the 107 buses purchased in that year. By August of 1960 there had been accumulated in the reserve for depreciation 49% of the investment (7 years times the annual rate of 7%). If the Company then reduces the annual rate of depreciation for that bus to 5.74%, it will take only approximately 8-1/2 years to accumulate the remaining 48.5% of investment not recovered. (The net investment to be written off, after allowance for salvage, is 97.5%.) As a result the bus will be written off in 15-1/2 years instead of 17 years.

On the other hand, if the annual rate of 5.74% is applied for 10 years subsequent to August of 1960, the total accumulated depreciation at the end of 17 years will be 106.4% of the gross investment (49% over first 7 years plus 57.4% over last 10 years). Either application produces an undesirable and inequitable result. It is clear that the undepreciated



investment in a bus must be depreciated over the remaining life to 17 years. This method was followed by the Chief Accountant in computing the adjusted amount of depreciation applicable to buses and in our opinion is the only proper way to effect the transition to the new annual rate of depreciation.

In consideration of the above, the Commission finds that with the reduction in the rate of depreciation applicable to buses, as was ordered, and the reduction in the rate of depreciation applicable to limousines, together with the retention of the remaining rates of depreciation applicable to the balance of depreciable plant and the special amortization of certain rail facilities, a proper and adequate annual accrual for depreciation will result.

If the present depreciation reserve is adequate, as determined, and the annual accrual is sufficient, as demonstrated, then it inevitably follows that a proper amount of depreciation has been charged and is being charged. This situation will obtain until August of 1963 at least, when the special amortization terminates. At that time the operation should be an all bus operation, and at that time it would be advisable to review the depreciation reserve and annual rates again in the light of the changed situation.

The Commission has carefully considered the report offered by Mr. Ingoldsby, together with the supporting schedules and charts, and takes note that a most comprehensive and objective study was made. The study was submitted to the Company for consideration and analysis and although the Company was not in accord with certain of Mr. Ingoldsby's recommendations, no errors were developed. All of the significant items of plant are discussed in detail and a full explanation set forth of the procedures followed.

A comparison of the depreciation rates established by Order No. 4001, effective July 1, 1953, and the rates developed by Mr. Ingoldsby at this time follows:

<u>Class of Property</u>	<u>Rate per Order No. 4001</u>	<u>New Rate Recommended</u>
Buildings and Structures	2.5%	2.6 %
P.C.C. Type Streetcars	4.2	4.6
Accessory Equipment for Streetcars and Buses	3.2	3.2
Rail Service Equipment	2.1	2.3
Passenger Buses	7.0	5.74
Track and Line	3.2	3.3
Duct System	2.6	3.7
Low Tension Cable	1.9	3.0
Substation Equipment	2.2	2.3
Shop, Carhouse and Garage Equipment	3.6	3.6
Tools and Work Equipment	4.8	4.8
Automotive Service Equipment	6.8	7.2
Communication Equipment	4.8	10.0
Furniture and Office Equipment	4.5	5.5

In addition to the above, the Company had been depreciating charter limousines at an annual rate of 25%, which Mr. Ingoldsby has determined should be decreased to 20%.

In summary, the Ingoldsby study contemplates a reduction in the annual rate for buses from 7.0% to 5.74%, a reduction in the rate for charter limousines from 25% to 20%, the elimination of the special amortization in the amount of \$295,500 annually, and small increases in several other accounts.

In view of the pending retirement of all rail facilities, the Commission is of the opinion that a revision in the rates of depreciation for items of plant that will soon be abandoned is not desirable if the ultimate retirement loss can be provided for in a more convenient manner. It has been pointed out that the retention of the present rates of depreciation for rail facilities, coupled with the retention of the special amortization, will, when added to the lowered depreciation on buses and limousines, produce approximately the same aggregate amount of depreciation expense as the recommendation of Mr. Ingoldsby. The Commission is of the opinion that such a procedure is a more practical way to effect the indicated result.<sup>B</sup>

A study such as the one made by Mr. Ingoldsby in this matter is at best a theoretical study which offers indicators as to the adequacy of past depreciation practices, and guides to the annual requirement under present conditions. As the reserve for depreciation of D. C. Transit is not segregated by class of property, and also because the group method of depreciation is being followed for all items of plant except buses, it is not important that the annual rate for each class of property be prescribed precisely. It is important that the total amount of depreciation accumulated to date is reasonably adequate, and the total annual charge is sufficient, but the means to accomplish that objective may take several paths.

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<sup>B</sup>The Franchise of D. C. Transit requires it to initiate and carry out the conversion of its street railway operations to bus operations on or before August of 1963. Mr. Ingoldsby used that date as a basis for his computation of rates of depreciation applicable to plant items that will be abandoned upon final conversion. August 1963 is also the termination of the special amortization of rail facilities that were abandoned coincidentally with the conversion of January 1960. In the event all or part of the presently existing rail facilities are abandoned prior to August of 1963 there need be no new provision for special amortization or acceleration of applicable rates of depreciation.



It must be noted that depreciation applicable to buses, which is by far the largest item of plant and the most critical, has already been adjusted to the indicated level. The problem of adequate accruals of depreciation for rail facilities will soon be eliminated. As the Commission has already taken one step to provide adequate reserves by establishing the special amortization heretofore discussed, it appears desirable to continue that program to its conclusion unless it now appears to be unrealistic. To eliminate that charge and offset the reduction by increasing rates applicable to the remaining rail facilities for a span of approximately 2-1/2 years does not appeal to the Commission when the same end result can be accomplished in a simpler manner.

#### Findings and Conclusions

1. That the establishment of a service life of 17 years for buses as heretofore found is proper and reasonable.
2. That the annual rate of depreciation applicable to buses, including spare parts and accessories, of 5.74%, based upon a service life of 17 years with allowance for net salvage of 2.5%, heretofore established by the Commission in its Order No. 4735, is proper and adequate.
3. That the unit method of depreciating buses, including spare parts and accessories, is proper and adequate.
4. That the special amortization of abandoned rail facilities in the amount of \$24,625 per month, established by Order No. 4631, Formal Case No. 471, be continued to its conclusion.
5. That the annual rate of depreciation heretofore applicable to limousines of 25% shall be terminated as of February 28, 1961.
6. That on and after March 1, 1961, the annual rate of depreciation applicable to limousines shall be 20%.
7. That the group method of depreciation heretofore applicable to limousines shall be terminated as of February 28, 1961.
8. That on and after March 1, 1961, the unit method of depreciation applicable to limousines shall be utilized.
9. That annual rates of depreciation applicable to items of plant other than buses, bus spare parts and accessories, and limousines, remain at their present level.
10. That the retention of the special amortization of abandoned rail facilities, together with the reduced annual rate of depreciation applicable to buses, bus spare parts and accessories, and limousines, and with the continuance of the present rates of depreciation applicable to the balance of plant, will produce annually the amount of depreciation accrual estimated to be necessary.

11. That the accumulated reserve for depreciation to date is adequate and no adjustment thereof is indicated or necessary.

12. That adjustment of the monthly charges for depreciation applicable to limousines since March 1, 1961, be effected by recomputing such depreciation charges on the basis of remaining life to the established minimum of 60% of investment over a 3-year service life.

NOW, THEREFORE, IT IS ORDERED:

Section 1. That the annual rates of depreciation applicable to the various classes of property of D. C. Transit as shown below are proper and adequate:

<u>Class of Property</u>	<u>Rate for Annual Depreciation Accruals (Percent)</u>
Buildings and Structures	2.5
P.C.C. and Streamline Type Streetcars	4.2
Accessory Equipment for Streetcars	3.2
Rail Service Equipment	2.1
Locomotives	3.5
Passenger Buses, including Spare Parts and Accessories	5.74
Limousines	20.0
Track and Line	3.2
Duct System	2.6
High Tension Cable	1.5
Low Tension Cable	1.9
Substation Equipment	2.2
Shop, Carhouse and Garage Equipment	3.6
Tools and Work Equipment	4.8
Automotive Service Equipment	6.8
Communication Equipment	4.8
Furniture and Office Equipment	4.5

Section 2. That the unit method of depreciation be utilized by D. C. Transit for depreciating its investment in buses and limousines.

Section 3. That appropriate adjustment of the monthly charges for depreciation applicable to limousines subsequent to the effective date of this Order be effected via the application of the remaining life method in conformance with the establishment of a 3-year service life and net salvage of 40%.

Order No. 4754, page 10.

Section 4. That the Company submit to the Commission copies of the adjusting entries required to be made by Section 3 above without unnecessary delay.

Section 5. That the effective date of this order is March 1, 1961.

A TRUE COPY:

By the Commission:

Chief Clerk

Norman B. Belt  
Executive Secretary

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

United States Court of Appeals  
for the District of Columbia Circuit

FILED FEB 13 1962

*Joseph W. Stewart*

CLERK

No. 16,454

-----  
Leonard N. Bebchick, and  
Leonard S. Goodman

Appellants:

vs.

Public Utilities Commission of  
the District of Columbia, and  
D.C. Transit System, Inc.

Appellees  
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APPELLANTS SUPPLEMENTAL MEMORANDUM

This memorandum is supplied in response to a query by Judge Danaher during argument as to the significance in amount of the different items challenged by appellants.

A. Increase In Revenues

The entire amount of the cash fare increase granted by the Commission provides an increase in gross operating revenues of \$1,163,823, and a corresponding

increase in net operating income (after taxes) of \$483,103. <sup>1/</sup>

1. The Commission calculated that the existing 20¢ cash fare would have provided Transit with gross revenues in the amount of \$26,708,655 (JA-2), enabling Transit to cover all expenses, including charges contested by appellants, and to earn a net operating income (after taxes) of \$660,146 to provide for interest payments of \$317,000 and a return to stockholders of \$343,146 (JA-10). This return equals 12.83% of Transit's equity, which is \$2,671,389 (JA-60).

2. In permitting an increase in the cash fare to 25¢, the Commission calculated that Transit would realize gross operating revenues in the amount of \$27,872,478 (JA-2), enabling Transit to fully cover all expenses, including the contested expenses, and to earn a net operating

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1/ This increase in net operating income under the 25¢ fare results after adjustment for the increase in income taxes and for an increase in the annual accrual for the Injury and Damages Reserve which is calculated as a percentage of gross operating revenues (See Commission Exhibit No. 40, reproduced in Brief of Transit at p. A-33).

income (after taxes) of \$1,143,249 to provide for interest payments of \$317,000 and a return to stockholders of \$826,249 (JA-2), a return of 30% on equity.

B. Expense Items Contested by Appellants

The following shows the size of the expense items contested by appellants, and their effect (assuming they were not properly treated as expenses) in increasing annual net operating income (after taxes) to Transit above the amounts contemplated even by the Commission.



<u>Operating Expenses</u>	<u>Refer- ence</u>	<u>Amount</u>	<u>Resulting Increase In Net Operating Income (after in- come taxes)<sup>2</sup> /</u>
1. Reserve for Track Removal & Repaving (provided annually for the period 1956-1966)	JA-51	\$1,044,196	\$477,198
2. Depreciation expense for rail properties aban- doned on January 3, 1960			
- Annual depre- ciation at nor- mal rates (49.5% of \$933,596)	JA-52	461,183	210,901
- Special annual amortization (provided an- nually for period 1960- mid 1963)	JA-52	295,500	135,044
3. Depreciation ex- pense on fully depreciated buses	JA-71 Adj. D.	246,253	112,538
Total expense disallowed		<u>\$2,047,143</u>	
Total Increase in net operating income (after taxes) resulting from disallowance			<u>\$935,681</u>

<sup>2</sup> / Transit's income tax rate, rounded, is 54.3%. This reflects a 52% Federal rate with credit given for D.C. taxes at 4.6% and Maryland taxes at .2225% (JA-67, 72).

At an effective tax rate of 54.3%, the disallowance of an operating expense results in increasing net operating income (after taxes) by an amount equal to 45.7% of the disallowed expense.

C. Relative Relationship of Challenged Items

The foregoing amounts show that, even assuming (arguendo) the propriety of the Commission's increase in the return to Transit stockholders by the amount of \$483,103, an equivalent increase results from disallowance of the track removal accrual as a current expense, or from disallowance of the depreciation accruals for abandoned rail properties and fully depreciated bus properties.

Thus, appellants conclude not only that the Commission should have withheld any fare increase but also that Transit had ample income available to absorb post-1960 cost increases.

Acceptance of appellants' contention regarding either group of operating expenses or its contention regarding the excessiveness of the return accorded by the Commission makes it clear that the 25¢ cash fare was invalid. As prayed by appellants (Brief p. 71), this Court should order the District Court to provide that the amounts unlawfully collected, 5¢ on each cash fare, be held for the benefit of farepayers by being funded and segregated in

a special Reserve which would be available as the Commission may require -- in lieu of fare increases -- to absorb any future wage or other increased operating expenses.

Respectfully submitted,

  
Harold Leventhal

  
Leonard N. Bebchick

  
Leonard S. Goodman

Dated: February 12, 1962

Attorneys for Appellants

CERTIFICATE OF SERVICE

I certify that copies of Appellants Supplemental Memorandum were mailed, postage prepaid, to Harvey M. Spear, Esq., counsel for appellee D.C. Transit, 3600 M Street, N.W., Washington, D.C., and to George F. Donnellia, Esq., counsel for appellee Public Utilities Commission, District Building, Washington, D.C., this 12th day of February, 1962.

  
Leonard N. Bebchick

**UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT**

**No. 16,454**

*Filed*  
United States Court of Appeals  
for the District of Columbia Circuit

**FILED JUL 27 1952**

*Joseph W. Stewart*  
**CLERK**

**LEONARD N. BEBCHICK, AND  
LEONARD S. GOODMAN**

**APPELLANTS**

**VS.**

**PUBLIC UTILITIES COMMISSION OF  
THE DISTRICT OF COLUMBIA, AND  
D. C. TRANSIT SYSTEM, INC.**

**APPELLEES**

**APPELLANTS' PETITION FOR REHEARING EN BANC**

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**ATTORNEYS FOR APPELLANTS**

UNITED STATES COURT OF APPEALS  
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Leonard N. Bebchick, and  
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Appellants

v.

Public Utilities Commission  
of the District of Columbia,  
and D. C. Transit System, Inc.

Appellees

---

No. 16,454

APPELLANTS' PETITION FOR REHEARING EN BANC

Appellants respectfully request rehearing of this case by the Court en banc because of the importance of the issues presented and the serious errors contained in the Court's opinion.

I

SUMMARY

On July 12, 1962, a divided panel, Judge Fahy dissenting, affirmed the decision of the District Court which sustained an Order and Opinion of appellee Commission increasing the cash fares charged Transit riders in the District of Columbia.

The Court's decision rests upon false assumptions and completely fails to analyze the actions of the Commission, relying merely upon the verbal rationalizations contained in the Commission's Opinion. The Court ignores the substantial evidence of record and further announces an unprecedented doctrine of immunity from judicial review.

The failure of the Court to provide a meaningful judicial review permits the Commission:

- a. to allow the Company to charge farepayers over \$1 million annually for track removal costs contrary to the uncontradicted evidence that the accrual is based upon wholly erroneous assumptions and that the amounts are not required;
- b. to permit the Company to charge farepayers double depreciation on admittedly fully depreciated bus properties;
- c. to permit the Company to charge the farepayers depreciation on abandoned rail properties not used and useful in the public service, contrary to principles established by this Court;
- d. to permit the Company to earn a return which is grossly excessive and whose reasonableness the Court has not even attempted to examine in light of the evidence of record.



## II

### STATEMENT OF THE CASE

This is an appeal from a decision of the appellee Commission allowing the transit company to increase its cash fares in the District of Columbia from 20 cents to 25 cents, effective March 6, 1960. The District Court originally dismissed the appeal on the grounds that appellants were without standing to maintain their suit. This Court reversed in Bebchick v. Public Utilities Commission, 109 U.S. App. D.C. 298, 287 F 2d 337 (1961). On remand, the District Court denied appellants' motion for summary judgment, finding there were "material issues of fact existing in the case" (see JA 39). On petitions for reconsideration by the parties, the District Court entered a conclusory order affirming the decision of the Commission (JA 39). The present appeal followed which resulted in a decision by a divided panel affirming the judgment below, Judge Fahy dissenting.

## III

### THE IMPORTANCE OF THIS PROCEEDING

This appeal raises a basic question as to the propriety of regulatory procedures by which transit rates are established in the Washington Metropolitan Area. The

interests of over one million transit riders residing with-  
in three jurisdictions are directly at stake.<sup>1/</sup> We believe  
that fundamental standards of rate making and prior de-  
cisions of this Court are being flagrantly violated; a  
justice of this Court agrees.

This petition, in addition, presents the vital  
question of whether consumers are to receive meaningful  
judicial review as contemplated by Congress. We believe  
that the succeeding portions of this petition amply demon-  
strate that such judicial review remains to be accorded.

The majority decision in substance proclaims that an  
indulgent attitude towards the utility by the Commission,  
characterized by a glossing over of the record with bare  
generalities and indefinite allusions to possible future  
study, will in turn be tolerantly indulged by the Court.  
By-passed are the transit riders.

The unfortunate and far-reaching consequences of the  
majority's decision are underscored by the difficulties  
confronting representatives of the public who undertake to

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<sup>1/</sup> The rate-making power exercised by appellee Commission  
has been transferred to the Washington Metropolitan Area  
Transit Commission with jurisdiction over the District  
of Columbia and portions of Maryland and Virginia; all  
outstanding Orders and Regulations of appellee Com-  
mission, including those here challenged, were continued  
in effect and remain unchanged (74 Stat 1931, Sec. 21).

provide a type of economic and legal analysis which the Commission is otherwise content to by-pass. When the Company is "injured" by Commission action, the matter can be readily litigated and re-litigated. But on the infrequent occasions when consumer representatives are able to muster forces to demonstrate obvious and serious improprieties, they should not be brushed aside by vague promises of study in the indefinite future.

#### IV

##### THE BASIC ERROR OF THE MAJORITY

In reaching its decision, the majority of the divided panel failed to undertake the scope and type of review which Congress has decreed (District of Columbia Code, Title 43, Section 706). The Commission's actions are upheld on two grounds.

First, the Commission's decision is said to set forth "'a suitably complete statement' of its reasons for its conclusions". In support of this portion, the majority quotes extensively from the opinion of the Commission. But judicial review of the issues here presented is not accomplished simply by ascertaining whether an agency's attempted rationalizations of its actions are stated in nicely phrased language. The Court is required to pierce the verbal veil and to ascertain precisely what the

Commission has done and whether such actions are contrary to established legal standards or are unsupported by the substantial evidence of record. This, we respectfully submit, the majority has failed to do.

Secondly, the majority in the next to last paragraph of its opinion, announces a novel and unfortunate doctrine of immunity from judicial review. The Court in effect excuses actions contrary to the record on the ground that a new Congressional franchise for transit operations, having replaced an older one (in 1956), the regulatory body has virtually unlimited leeway so long as it intones a "promise" to "study the situation and make such adjustments as time may require".

The concept of an "experimental" approach has no valid application to justify a rate increase where the uncontradicted record shows that the utility's claimed expenses are not admissible. There is no warrant for tolerating a rate increase on assumptions which find no support in the record and indeed are contradicted by the record.

This novel avoidance of judicial review should not stand as the law of this jurisdiction. Congress has taken no action to so limit review by this Court in these appeals.

The Commission's patent errors compel the Court to take immediate corrective action. Transit riders can

obtain the protection to which the law entitles them only if this Court provides meaningful judicial review.

V

THIS ILLEGAL ACTIONS OF THE COMMISSION

A. The Commission committed serious error in permitting the Company to continue to accrue as an operating expense over \$1 million annually for a ten-year period to provide for the cost (before taxes) of track removal and repaving.

Petitioners believe that none of the costs of track removal and repaving should be borne by transit riders, as the Company has already been compensated for these prospective costs which are in the nature of a capital item. Transit's investors purchased the assets of the predecessor Company for a \$10 million discount under the depreciated book value. There is abundant evidence of record, as summarized in the dissenting opinion, that this discount was given to compensate the Company for the obligations assumed under its Congressional Franchise to convert to an all-bus operation within seven years. Judge Fahy concluded that the prospective cost of track removal was an important factor in arriving at the Company's purchase price; he would remand to the Commission for a careful investigation of the nature of the discount so that a fair division of its

benefits could be made between the investors and farepayers. The majority completely ignored this pivotal point.

Secondly, even assuming arguendo that farepayers should be burdened with the capital costs of track removal, the record makes it plain that the amounts which the Commission is permitting the Company to accrue are grossly excessive. Again, the salient facts are summarized in Judge Fahy's dissenting opinion. The \$1 million annual accrual is based upon an estimate of a total cost of track removal (without consideration of the corresponding reduction in income taxes) of some approximately \$10.5 million. But it is clear that this figure assumes that the company will bear the full costs of removing all the tracks and repaving the track area. However, both the Company's Franchise and the D. C. Appropriation Act of 1942 contemplate that track removal and repaving will be accomplished in conjunction with the District of Columbia Highway Department's road maintenance program with a required 50% sharing of repaving costs between the District and the Company. Moreover, considerable portions of the trackage will not be removed but will be merely covered over by asphalt at substantial reductions in cost.

Thus, there is no warrant in the Commission's action in permitting further accruals, particularly in light of



the Company's inability to provide any estimate of its actual expenditures within the foreseeable future. (JA 249, 250). As of the time the Company filed for the rate increase here challenged, it had accrued as operating expense approximately \$3 million and had expended only some \$61,338! On the basis of the evidence of record, the Commission's continued sanction of \$1 million annual accrual was arbitrary and contrary to the evidence.

In treating this point, the majority place reliance upon what has become the Commission's standard response to challenge -- it will keep the matter under study with a view to making future adjustments as may appear warranted. On the basis of this record, petitioners submit that Judge Fahy is correct that it is necessary for the Commission to reappraise the track removal accrual without further postponement. Moreover, the Commission's action in a subsequent rate case demonstrates that meaningful review by this Court cannot be based upon reliance upon vague "promises" by the Commission.

In the subsequent proceeding, the Director of the D. C. Highway Department testified that the Company's total cost for track removal through fiscal 1966 (the end of the ten-year accrual period) would be approximately \$3 million unless the Commission itself ordered an acceleration in the

program. As of this time, Transit had already accrued over \$4 million for track removal. Thus more than enough money had been exacted from the transit riders to pay for the costs of track removal for the next six years. Yet the Commission blithely permitted the Company to continue accruing \$1 million annually, although it indicated that it would continue to keep the matter under study! (Re. D.C. Transit System, 38PUR3d, 19, 42-44 (1961)). Such an established pattern of inaction is hardly a proper substitute for sound regulation or meaningful judicial review.

B. The Commission erred in permitting the Company to accrue depreciation of approximately \$250,000 for buses which already had been fully depreciated. The Commission depreciates buses as a group at a rate which assumes a service life of 14 years; buses are retained in the group until they are actually retired from service. Yet the overwhelming evidence of record indicated that buses are never retired prior to 14 years of life (except in the infrequent case of accident), and that the average service life is substantially higher (e.g. JA 47). The result is that transit riders are required to provide depreciation expenses with respect to fully depreciated buses; i.e. on those 300 buses over 14 years of age. Indeed the Company had already accrued some \$1.2 million of such excess

depreciation as of this proceeding (JA 15). Here again the Commission justified its continued allowance of double depreciation upon the need for a study and the majority of the panel concurred. But as Judge Fahy pointed out, while the suggestion of further study is advisable, this does not justify the continued allowance of this "artificial" expense deduction with the end result that increased fares are required to maintain the Company's net operating income at a particular level. Petitioners merely urged the Commission to discontinue the allowance of double depreciation on fully depreciated buses pending such a study; a step hardly injurious to the Company in view of surplus depreciation already accrued in an amount five times greater than the challenged accrual for fully depreciated buses.<sup>1/</sup>

C. The Commission also erred in permitting the continued depreciation at normal rates and imposing an additional special amortization allowance with respect to street rail properties which had been abandoned and were no longer used and useful in the public service.

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<sup>1/</sup> It is instructive to note that the Commission abandoned its group method of bus depreciation in a subsequent proceeding. (Re, D. C. Transit System, cited supra). Yet even here, the Commission required Transit riders to pay double depreciation on buses for one-half of the future test period. As Judge Fahy notes, the subsequent action by the Commission merely confirms the impropriety of its actions in this proceeding.

On January 3, 1960, the Company had abandoned \$2.5 millions (approximately 50% of its rail facilities. Yet the Commission permitted the Company to continue to accrue depreciation at normal rates on these abandoned properties. Moreover, in order to assure that the abandoned properties would be fully depreciated by 1963 (the then anticipated date of complete conversion from rail to bus), the Commission permitted the Company to accrue an additional annual amount of \$295,000 as a special amortization allowance.

This Court has established that depreciation on abandoned properties is permissible only if the investors have not been compensated for assuming the risk that the properties would be abandoned before the investment was entirely recovered (Washington Gas Light Co. v. Baker, 88 US App. D.C. 115, 188 F2d, 11, cert. denied, 340 US 952).

As noted earlier, the Company received a discount of \$10 million when it purchased the assets of the predecessor Company. The evidence establishes that this discount was paid to compensate the new investors for the obligation undertaken to convert to bus operations and to remove existing trackage. Petitioner's expert witness testified that the \$10 million discount was adequate to provide both for the undepreciated values of abandoned rail properties and, in addition, the costs of track removal and repaving.

Judge Fahy would also have reversed on this point which he recognized was "a matter of substance . . . not merely a question of findings". Given his desire for further Commission clarification as to the circumstances surrounding the discount, he could not conclude as to precisely in what manner and in what amounts the \$10 million discount should have been applied to reduce amounts otherwise charged transit riders for track removal and for depreciation on abandoned properties. Petitioners believe that the evidence of record supports their position that the Company and its investors have been compensated for all costs of conversion, and that transit riders should not be required to pay for any such expenses (e.g. JA 67). Be that as it may, the logic of Judge Fahy's reasoning is inescapable - the Commission may not totally disregard the discount and yet compel transit riders to provide Transit's investors with double compensation. As the dissenting opinion indicates, "Unless a very substantial part of this very substantial sum is taken into account in reducing the annual accrual for track removal and repaving . . . it must be taken into account in arriving at the allowance for depreciation on these abandoned rail properties".

In Petitioners' view, the majority, completely fails to consider this point in its disposition of the rail



depreciation issue. Indeed, it begins by assuming that Transit is entitled to recover the undepreciated costs of abandoned properties and considers the matter as if Transit had claimed that it is entitled to recover more than the Commission has allowed! It is in this context that the Commission's allowance is upheld as reasonable.<sup>1/</sup>

D. The Court acquiesces, without any examination, in the Commission's action permitting Transit to earn income (after all expenses and taxes) in excess of \$1 million annually. This return is computed by the Commission to be 4.1% of gross operating revenue and 7.14% of system rate base. The Commission states that it "utilizes" its estimate of income as a percentage of system rate base to "test" the

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<sup>1/</sup> Here again, the Commission promises a future study. But it has not yet undertaken the type of study which Judge Fahy felt immediately required and which of necessity would compel a modification of some of the practices here challenged. The basic point, however, is that no depreciation accruals for abandoned properties are justified; studies such as the Commission engages in are relevant only if it is mistakenly assumed that the investors have been compensated for the risks of obsolescence.

It is, however, interesting to contrast the Commission's precipitous adoption of the special amortization allowance in the absence of study, with its refusal to eliminate admitted double depreciation on fully depreciated buses until a study has been completed. The impropriety of allowing special amortization is reinforced by the Commission's admissions (a) that its present estimates of the undepreciated value of abandoned properties is probably outdated and that a current study might well result in a different valuation and (b) that large surplus amounts in the bus depreciation account could be utilized to offset such unrecovered depreciation.



return as expressed in terms of a percentage of gross operating revenues.<sup>1/</sup> The "test" consists merely of arithmetically expressing the dollar amount of the return otherwise selected as a percentage of the rate base; the Commission does not engage in any of the inductive procedures by which the "rate-base-rate-of-return" standard normally is employed as an actual method for arriving at a determination of fair return. (See Capital Transit Company v. Public Utilities Commission, 93 U.S. App. D.C. 194, 213 F2d. 126, 186 (1953)).

The Commission does recognize that the Company under its Franchise is permitted to earn a return whose end result will enable it to cover its expenses and its costs of debt and equity capital (A JA 11);<sup>2/</sup> its recognition of a

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<sup>1/</sup> The gross operating revenue "method" involves nothing more than expressing the amount of net income earned as a percentage of revenues. The Commission concedes that "there is no formula or method for determining what constitutes a fair return on gross operating revenues"; such return must be the sole "result of Commission's judgment" (JA 11, 24).

<sup>2/</sup> The majority of the panel ambiguously quotes from Section 4 of Transit's Franchise without even citing the traditional attraction of capital return standard embodied therein which provides that Transit "should be afforded the opportunity of earning such return as to make the Corporation an attractive investment to private investors". The panel merely quotes from the following sentence regarding a 6-1/2% return which is operative only "as an incident" to the capital attraction standard and relates to the subsidy provisions of Section 9.

fair return from the consumers standpoint is less clear. But, the Commission must demonstrate that the end result of the earnings allowed is in fact reasonable in terms of the actual capital needs of the Company and the demands made upon the farepayers. (City of Detroit v. F.P.C. 97 U.S. App. D. C. 210, 230 F2d 810 (1955) cert. denied 352 U.S. 829 (1956)).

The Court does nothing more than repeat and ratify the conclusory findings by the Commission of fair return, findings which, we submit, are based upon undocumented and unsupported "judgment". There is no inquiry as to the basis on which the Commission reached such conclusions, of the evidence underlying the Commission's "methods", nor of the reasonableness of the end result in light of the balancing interests of the Company and the public. The review function is hardly exhausted by noting that a certain return on revenues has been arithmetically described as a certain return on rate base, even assuming that the process of restating has been done properly.<sup>1/</sup> The question remains as to why the particular percentage of return is a reasonable one. A meaningful judicial review is yet to be accomplished.<sup>2/</sup>

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<sup>1/</sup> Appellants demonstrate serious errors in the Commission's determination of system rate base Brief, pp. 39-60.

<sup>2/</sup> Judge Fahy did not reach the adequacy of the return permitted by the Commission as he found that the excessive expense deductions sanctioned by the Commission materially affected Transit's net income and the justification for the fare increase (see Appellant's Supplemental Memorandum, dated February 12, 1962, submitted upon request of Judge Danaher).

This Court has established that a judicial inquiry must be made to determine whether the Commission employed a rational process to reach its result and whether such a series of basic findings, if they are found in the Commission's opinion, comport with the substantial evidence of record. As this Court states in the Washington Gas Light Co. v. Baker, cited supra, "Commission expertise alone cannot support so pivotal an assumption . . . Without any evidence on this essential issue, there is no basis for application of any standard and the judicial review authorized by the statute becomes a formal but futile gesture."

The Commission relied exclusively upon the testimony of its staff witness Falk to find that 4.10 percent of revenues (or its corollary 7.14 percent on the system rate base) was a fair rate of return (JA 24-25). But this witness made no comparative or individual company study of Transit's return needs (JA 145-148). He testified he had "made no studies of other transit companies" as to fair return (JA 147); and when asked, "and no statistical or analytical studies premise this conclusion of yours" relating to the fair return, he replied "That is correct". (JA 148).

On the other hand, the substantial evidence clearly showed that earnings under such rates of return would be

excessive. The return necessitates a cash fare of 25% greater than the national average or medium. It permits the utility to maintain an annual dividend of 100 percent of its capital stock investment (see JA 24 and 49) and, more significantly, earnings on equity capital of 30 percent (JA 25). There was substantial comparative statistical evidence introduced by intervenors that a return of 12 to 13 percent on equity would be reasonable (JA 56-60). Moreover, past earnings have been excessive; in the first three years of the Company's life, it paid out dividends of over \$1 million on an equity investment of \$500,000 (JA 65), and the average annual return on equity was 95.92 percent (JA 66).

Thus, there is an urgent need for the Court to scrutinize in light of applicable standards the Commission's conclusions as to fair return which rest only upon an undocumented and unsupported "judgment".

VI

PRAYER

For the foregoing reasons, appellants submit the Court's discretion would be appropriately exercised in ordering rehearing en banc.<sup>1/</sup>

/s/ Harold Leventhal  
Harold Leventhal

/s/ Leonard N. Bebchick  
Leonard N. Bebchick

/s/ Leonard S. Goodman  
Leonard S. Goodman

Attorneys for Appellants

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<sup>1/</sup> Appellants will undertake to provide such additional copies of their mimeographed Briefs as the Court may desire.

**CERTIFICATE OF GOOD FAITH**

We certify that this petition is presented in good faith and not for delay.

/s/ Harold Leventhal

Harold Leventhal

/s/ Leonard N. Bebhick

Leonard N. Bebhick

/s/ Leonard S. Goodman

Leonard S. Goodman

Attorneys for Appellants

**CERTIFICATE OF SERVICE**

I certify that a copy of the foregoing Petition was mailed, postage prepaid, to Harvey M. Spear, counsel for appellee Transit, 3600 M Street, N. W. Washington, D. C., and to George F. Donnellia, counsel for appellee Commission, District Building, Washington, D. C., this 27th day of July 1962.

/s/ Leonard N. Bebhick



~~OFFICE COPY~~

UNITED STATES COURT OF APPEALS  
For The District Of Columbia Circuit

\_\_\_\_\_  
No. 16,454  
\_\_\_\_\_

United States Court of Appeals  
for the District of Columbia Circuit

FILED AUG - 6 1962

LEONARD N. BEBCHICK, et al.,

*Joseph W. Stewart*  
CLERK  
APPELLANTS

v.

PUBLIC UTILITIES COMMISSION, et al.,

APPELLEES

\_\_\_\_\_  
PUBLIC UTILITIES COMMISSION'S OPPOSITION TO  
PETITION FOR REHEARING EN BANC

The points relied upon in appellants' petition for rehearing en banc were extensively briefed, urged during oral argument, and fully and correctly disposed of by this court in its opinion rendered in the above-entitled cause on July 12, 1962.

Perhaps one area might need clarification. Appellants would lead the court to believe that the Commission gave no consideration to the fact that the purchase price paid by Transit for the transportation system in the District of Columbia was some \$10,000,000 less than the book value

of the properties acquired. Appellants state at page 7 and 8 of their petition:

"Transit's investors purchased the assets of the predecessor Company for a \$10 million discount under the depreciated book value. There is abundant evidence of record, as summarized in the dissenting opinion, that this discount was given to compensate the Company for the obligations assumed under its Congressional Franchise to convert to an all-bus operation within seven years. Judge Fahy concluded that the prospective cost of track removal was an important factor in arriving at the Company's purchase price; he would remand to the Commission for a careful investigation of the nature of the discount so that a fair division of its benefits could be made between the investors and farepayers. The majority completely ignored this pivotal point."

Initially, appellants adopted the position of their witness that the reduced purchase price paid was based on writing off all rail facilities as being of no value. The Commission rejected this approach and stated:

"We fail to see how rail facilities could be considered as valueless when they had a remaining useful life of seven years and were at the time producing annual revenues of approximately \$12,000, - 000." (JA 16)

Although the Commission refused, for reasons stated, to adopt appellants witness's views with respect to rail values, the record clearly demonstrates that the \$10,339,041 acquisition adjustment, representing the differences between the book value of road and equipment acquired by Transit and the purchase price, was used in full measure by the Commission to reduce depreciation to the basis of purchase price on all items of

property acquired.

The Commission stated (JA 12-13):

"Briefly, the credit for amortization of acquisition adjustment in the amount of \$1,033,904 is the annual write-off of the total amount of \$10,339,041, which is the excess of depreciated original cost of road and equipment acquired by D. C. Transit System, Inc. from Capital Transit Company over that portion of the purchase price assignable to road and equipment. The record shows that the amortization of this excess over a ten-year period was adopted in lieu of distributing the purchase price of the property over all of the items of property acquired. That is to say, the property is recorded on the books of D. C. Transit System, Inc. at original cost to Capital Transit Company, in accordance with the provisions of the Uniform System of Accounts, and depreciation is accrued on the basis of original cost, with an offsetting credit for amortization of the acquisition adjustment to effectively reduce the provision for depreciation to the basis of depreciation of the purchase price of the property. We approved this procedure in the 1958 rate proceeding and in prior motor vehicle fuel tax determinations and find no reason for changing that position for purposes of this proceeding."

It would be difficult, if not impossible, to more clearly demonstrate that the Commission not only gave consideration to the reduced purchase price paid by Transit upon acquisition, but also gave the full benefit of the reduced price to the farepayers in the form of reduced depreciation in the total amount of \$10,339,041 to be written off annually in the amount of \$1,033,904.

It follows that no matter how individual opinions might differ as

to what factors should be weighed by the Commission as against the reduced purchase price, the entire reduction was utilized by the Commission for the benefit of the public. The reduction can be used but once, notwithstanding appellants' contentions to the contrary. It is the appellants, and not the court, who have "completely ignored this pivotal point."

It is respectfully submitted that the petition for rehearing en banc should be denied.

CHESTER H. GRAY  
General Counsel

GEORGE F. DONNELLA  
Counsel

ANDREW G. CONLYN  
Counsel  
Attorneys for Appellee, Public  
Utilities Commission  
District Building  
Washington 4, D. C.

#### CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Opposition was mailed, postage prepaid, this 6th day of August, 1962, to Harold Leventhal, Esq., 1632 K Street, N.W., Washington 6, D. C., attorney for appellants, and to Harvey M. Spear, counsel for appellee Transit, 3600 M Street, N.W., Washington, D. C.

GEORGE F. DONNELLA  
Counsel

235

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

LEONARD N. BEBCHICK  
and  
LEONARD S. GOODMAN

Appellants

vs.

No. 16,454

PUBLIC UTILITIES COMMISSION  
OF THE DISTRICT OF COLUMBIA  
and  
D. C. TRANSIT SYSTEM, INC.

Appellees

OPPOSITION OF APPELLEE, D. C. TRANSIT SYSTEM, INC.,  
TO APPELLANTS' PETITION FOR REHEARING EN BANC

United States Court of Appeals  
for the District of Columbia Circuit

FILED AUG 6 1962

*Joseph W. Stewart*  
CLERK

Harvey M. Spear  
Harold Smith  
3600 M Street, N. W.  
Washington 7, D. C.

Attorneys for Appellee,  
D. C. Transit System, Inc.

Dated: August 6, 1962

UNITED STATES COURT OF APPEALS  
FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

LEONARD N. BEBCHICK  
and  
LEONARD S. GOODMAN

Appellants

vs.

PUBLIC UTILITIES COMMISSION OF  
THE DISTRICT OF COLUMBIA  
and  
D. C. TRANSIT SYSTEM, INC.

Appellees

No. 16,454

OPPOSITION OF APPELLEE, D. C. TRANSIT SYSTEM, INC.,  
TO APPELLANTS' PETITION FOR REHEARING EN BANC

Appellee, D. C. Transit System, Inc., opposes appellants' Petition for Rehearing En Banc on the ground that appellants have failed to show any basis for such reconsideration.

FACTUAL STATEMENT

On February 8, 1962, this case came on for oral argument. More than five months later, on July 12, 1962, this case was decided. Judge Bastian wrote the majority opinion affirming the decision of the District Court sustaining an Order and opinion of the Public Utilities



Commission of the District of Columbia ("Commission")  
dealing with Transit fares. The majority opinion is now  
under attack by appellants.

QUESTION PRESENTED

Did the majority of the Court, in reaching its decision in Appeal No. 16,454, overlook any material fact or principle of law?

### ARGUMENT

Generally, an Appellate Court, in considering whether to grant or deny a Petition for Rehearing, is guided by a determination of whether or not a material fact or principle of law has been overlooked in reaching its initial decision. Where it is determined that there has been no such omission a rehearing will not be granted.\*

In this Petition, appellants are, in essence, doing nothing more than attacking the majority decision as being erroneous without the necessary showing of the overlooking of a material fact or principle of law. Appellants' Petition is a rehash of the exact same argument made in their Briefs and during the course of their oral argument. On separation of the wheat from the chaff, it becomes glaringly obvious that the real basis for this Petition is the fact that a dissenting opinion has been filed by Judge Fahy.

It is by no means rare or unusual to find a judge of the United States Court of Appeals for the District of Columbia disagreeing with his brethren. This Court has never held that the filing of a dissent, per se, is sufficient legal grounds for granting a Petition for Rehearing. Each judge

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\* North Carolina Utilities Commission vs. Norfolk Southern Railway Company, 224 N.C. 762, 32 S.E.2d 346; Crawford vs. Bach, et al., 101 N.E.2d 144; see also 5 C.J.S. 539.

is entitled to his individual opinion. However, Anglo-Saxon jurisprudence is founded on the principle that the majority will, and does, rule. Judges Bastian and Danaher carefully and painstakingly considered the identical record, briefs and oral argument, as did their brother, Judge Fahy. More than five months elapsed after oral argument before a decision was reached. It may be properly assumed that the record made before the P.U.C. was minutely examined, inspected, debated and discussed.

Appellants have time and time again, throughout this Petition, accused the majority of reaching its decision without consideration of the "substantial evidence of record." There is ample affirmative evidence in the majority opinion to indicate that careful and minute examination of the entire record was made by the majority.

Appellants' Petition for Rehearing En Banc reargues de novo all of the issues of fact in the same detailed manner as they reargued them before this Court at the original hearing herein and in the same manner as they reargued them before the District Court. Their Petition seeks to have this Court en banc consider de novo each of their proposed factual findings in order to have this Court substitute its findings of fact in place of the findings of

fact of the expert administrative agency involved herein, i.e., the Public Utilities Commission of the District of Columbia.

Appellants made the same error before the District Court and at the original hearing before this Court. The majority opinion herein duly pointed out the error. The error was and is in their assumption that this Court must en banc reconsider each of the factual findings from scratch as if the findings of the Commission were merely advisory. This assumption is directly contrary to the applicable law.

The extent to which this Court can reconsider the findings of the Commission are governed by Paragraph 66 of the Public Utility Law of the District of Columbia (Title 43, Section 706, D. C. Code), which provides:

"In the determination of any Appeal from an Order or decision of the Commission the review by the Court shall be limited to questions of law, including constitutional questions; and the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary, or capricious." (Emphasis supplied.)

Although this Court has often held that, in the absence of an unreasonable, arbitrary or capricious result, it will not substitute its judgment for that of an administrative agency, even if this Court might have reached

different conclusions from those of the administrative agency, nevertheless, it is not necessary in this case to go that far. In this case, the majority considered each of the controverted findings of the Commission and there was no disposition on the part of the majority even to reach different conclusions from those of the Commission. The reason is that the record of the proceedings before the Commission permitted only one set of conclusions. When all of the implications of each of the Commission findings are considered in the light of the complex origin and background of appellee, D. C. Transit System, Inc., the Commission findings are the only reasonable findings possible.

Specific Errors Alleged:

The Petition charges the majority with having erred in declining to find that the depreciation of rail properties by appellee, Transit, was unlawful. The District Court below and this Court examined the record before the Commission in detail, taking particular cognizance of the testimony of all witnesses on the issue. The majority noted the variance between the testimony of the Commission's witness and that of Transit's witness. The majority



affirmed the Commission's finding only after the aforementioned detailed study. Again, declining to substitute its judgment for that of the Commission, after careful consideration of the record, the Court found a reasonable basis for the Commission's finding, and acted correctly in refusing to set the same aside.

Appellants take issue with the majority's affirmation of the treatment accorded by the Commission to the matter of depreciation of bus properties. Here again the majority carefully considered the reasoning of the Commission and the evidentiary basis for the Commission's ruling. The majority agreed with the District Court and the Commission on the weight to be given to the testimony of appellants' witness on the question of bus depreciation. The Commission determined that it would not adopt the "novel" method proposed by appellants' witness. The Commission had a perfect right to weigh all testimony and to so decide. Appellants vigorously attacked the Commission's finding with regard to depreciation of bus properties both on oral argument and in their Brief. This Petition is devoid of any showing of legal error regarding the majority's affirmance of the Commission's finding as to depreciation of bus properties.

The majority affirmed the Commission's finding that the annual provision made by Transit for the cost of track removal and street repaving was justified on the basis of present experience. The majority agreed with the Commission that it would be necessary to keep the matter under continuing study with a view to making, in the future, such adjustments as might be found appropriate. Appellants allege that this affirmance constitutes error. It cannot be denied that Judge Fahy was of a different mind on this question. However, to reiterate, the difference of opinion standing alone, as it does here, is not a proper basis for granting a rehearing.

It must be recognized that at no point in the course of these proceedings, either before the Commission, the District Court, or the Court of Appeals, was there a factual situation presented to any of the foregoing bodies "on all fours" with the situation in the instant case regarding the stated intention of the administrative agency to continue to study and review the track removal and repaving factor. The situation is unique.

The Commission, the District Court and the majority of this Court recognized that circumstance. The Commission decided, in its expertness, and the majority

agreed, that the passage of time was a crucial factor to be considered in determining what method was to be used in arriving at an accurate amount to be set aside annually to provide for future track removal and street repaving. The majority found "there must be periods for trial - and error - but the Commission has promised to, and undoubtedly will, continue to study the situation and make such adjustments as time may require. As of the time of the Order under consideration, we are unable to say that the Commission has been unreasonable or arbitrary in the performance of its duties." In so deciding, the Court recognized the necessity for experimentation in unique situations such as that in the instant case. It is this recognition by the majority that is so vigorously attacked by appellants herein.

Appellants offer no support for their inferential argument that the Commission will pay nothing more than lip service to its avowed intention to continue the study. Appellants' attack, however, is unsupported by the showing of legal error by the Commission in the recognition of the need for time and experimentation. That the majority believes in the Commission's continuing study of the question, as promised by the Commission, is laudatory.

The majority of this Court concluded that the

Commission was correct in its determination as to the manner of computing Transit's rate of return and further concluded that the Commission was not unreasonable in computing the amount of Transit's rate of return on the basis of such computation. Appellants attack these conclusions. Appellants accuse the majority of blindly affirming the Commission without due consideration of the record before the Commission, and allegedly without proper judicial review of the reasoning underlying the Commission's conclusion.

A reading of the majority opinion leads to the unalterable conclusion that, contrary to appellants' argument, the Court undertook an intensive study and review of this specific question (pages 5-9, Opinion No. 16,454). The Court examined Transit's franchise and took particular cognizance of the exhibits introduced into the record on this issue. Included in the majority opinion of this Court is one of the detailed schedules introduced in evidence at the hearing before the Commission (Exhibits 39, J.A. page 53). Having taken pains to set out the aforementioned schedule, the majority then discoursed, at great length, on the subject of rate of return. Not even the dissenting opinion of Judge Fahy disagrees with the majority's conclusions as to the method of the computation of a rate of

return.

Even Judge Fahy stated that he agreed that "the Commission was authorized to adopt this [gross operating revenue] method." (Opinion, page 14, footnote 1.) On this point even Judge Fahy disagreed with appellants' arguments in their Petition for Reconsideration.

The majority took particular note of the fact that the Commission intended to and was using the "rate base-rate of return" method to test the reasonableness of the return computed under the gross operating revenue method. The Court considered the testimony of appellants' witness before the Commission, which was contrary to that of the Commission's witness, on the question of computation of rate of return. The mere fact that the Commission and the majority, after due consideration, refused to adopt the method and reasoning proposed by appellants' witness, is not the equivalent of demonstrating legal error upon which to predicate a rehearing.

In their Petition, appellants direct the Court's attention to a proceeding subsequent to the completion of the record before the Public Utilities Commission and upon which the majority based its opinion. This "subsequent proceeding" is outside of the record to be considered on



this Petition for Rehearing En Banc. It constitutes material which was not considered by the Court in reaching its decision. It is outside the scope of factors to be considered in arriving at a decision to grant or deny a rehearing.

The two cases cited by appellants in their Petition, Washington Gas Light Company vs. Baker, 88 U.S. App.D.C. 115, 188 F.2d 11, cert. denied, 340 U.S. 952, and City of Detroit vs. F.P.C., 97 U.S. App.D.C. 210, 230 F.2d 810, cert. denied, 352 U.S. 829, were also cited in their Briefs herein. The cases were given due consideration by the majority in arriving at its decision. Judge Fahy did not agree with the majority as to the weight to be accorded the Baker case, but this, in and of itself, is again merely a difference of opinion, and not proper grounds upon which to predicate the granting of a rehearing.

#### SUMMARY OF ARGUMENT

The majority of the Court, in arriving at a decision to affirm the Public Utilities Commission of the District of Columbia, accorded the full scale judicial review decreed by the applicable Statute. The majority analyzed and dissected the record before the Commission. It carefully scrutinized the reasoning of the Commission.

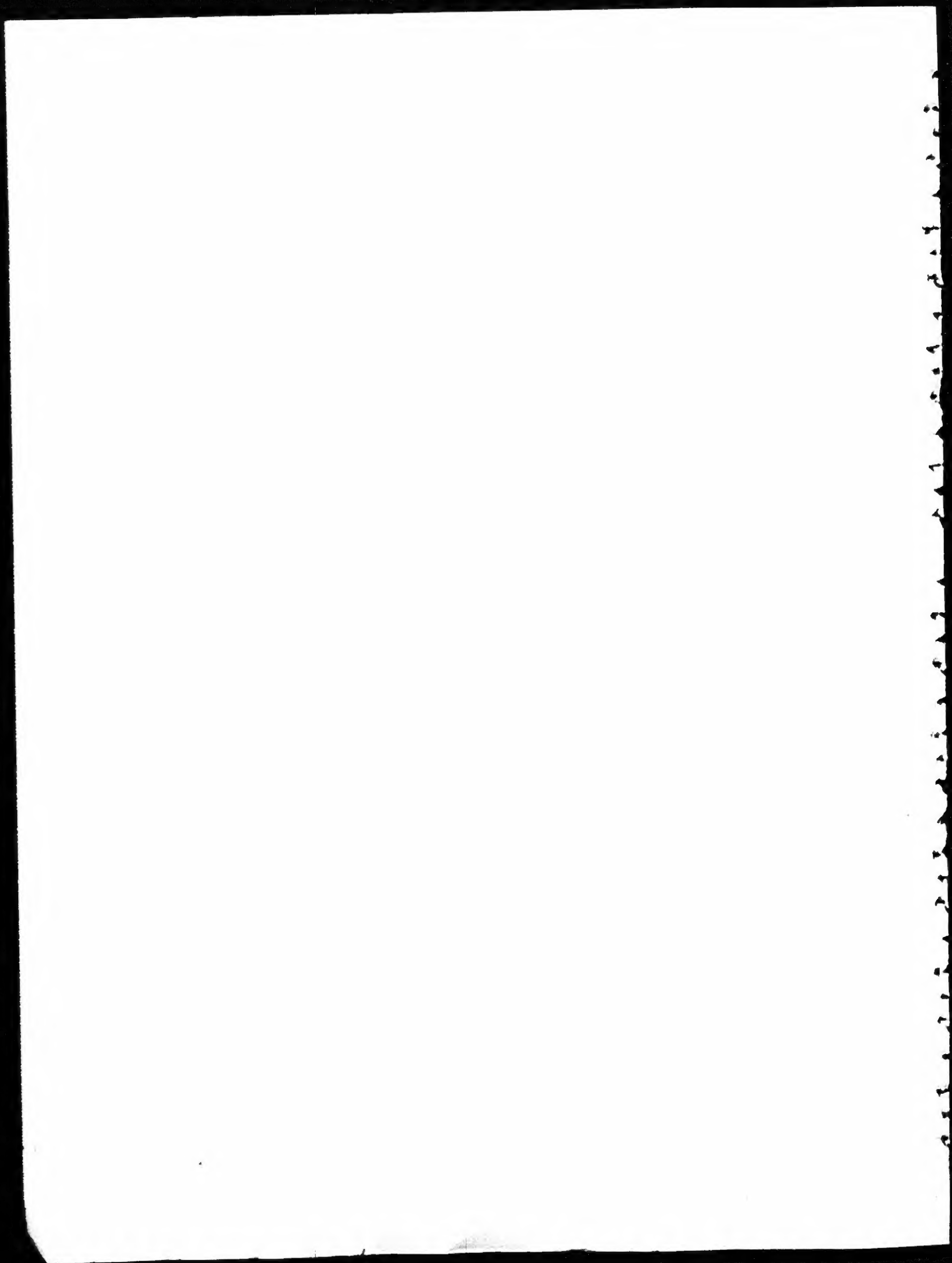


Regarding the question of future provisions for track removal and street repaving, the majority properly recognized the uniqueness of the situation confronting the Commission. It is this particular finding of the Commission which is so bitterly attacked by appellants herein. The majority, after due consideration, agreed with the Commission on the need for the passage of time to permit a measure of experimentation before a final solution of the particular problem is arrived at.

In reaching its decision on this and other questions hereinabove referred to, the majority made and completed a thorough study of the record. The majority decision is well grounded in logic and law.

Appellants would have this Court usurp the function of the Commission and invade its statutory jurisdiction. This the majority refused to do.

The majority correctly stated unequivocally, "We think the Commission's reasoning justifies its position, and we are not at liberty to substitute our judgment for that of the Commission." Appellants have failed to carry their burden of demonstrating to the Court that a material fact or principle of law has been overlooked or disregarded by the majority in reaching its decision to affirm.



CONCLUSION

For the reasons stated above, it is respectfully submitted that appellants' Petition for Rehearing En Banc should be denied.

Respectfully submitted,

/s/ Harvey M. Spear

Harvey M. Spear

/s/ Harold Smith

Harold Smith  
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CERTIFICATE OF SERVICE

A copy of the foregoing Opposition of Appellee, D. C. Transit System, Inc., to Appellants' Petition for Rehearing En Banc was mailed, postage prepaid, to Leonard N. Bebhick, Esquire, and Leonard S. Goodman, Esquire, Appellants, 1632 K Street, N. W. and 4336 River Road, N. W., Washington, D. C., respectively, and to George F. Donnella, Esquire, Attorney for Appellee, Public Utilities Commission, District Building, Washington 4, D. C., this 6th day of August, 1962.

/s/ Harold Smith

Harold Smith